BROADWAY
INVESTING 101

How to Make Theater
and Yes, Even Make Money

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Broadway Investing 101: How to Make Theater and Yes, Even Make Money
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DEDICATION

This book is dedicated to the hundreds and hundreds of investors who have helped me make theater happen. Thanks to you there is more theater in the world, which I believe makes the world a better place.

And we've even been able to make some money along the way.

For your support of the arts and of me, I'm forever grateful.

BROADWAY

INVESTING

TABLE OF CONTENTS

Special Thanks

When I started working on Broadway, there weren't a ton of books about the business. There were no blogs, no podcasts and no Google even (!), if you were interested in learning more about how to produce or invest in a Broadway show.

Back then there were just people.

Thankfully, I was blessed to be surrounded by some of the best and brightest on Broadway who taught me the mechanics of the business as well as the nuances of our industry that can't be put on a spreadsheet or a word document.

Some of these folks are mentors. Some are rock star Producers who gave me a job. Some are just terrific friends. Without their expert knowledge, shoulders to lean on and brains to pick, I couldn't have done half of the stuff I've done so far.

In no particular order, a special thanks to my attorney, Daniel M. Wasser at Franklin, Weinrib, Rudell & Vassallo, my Accountant Robert Fried of Withum, Nina Lannan, Barry and Fran Weissler, Robert Fox, Hal Luftig, Kristin Caskey, Ken Gentry, David Stone, Daryl Roth, Jeffrey Richards, Sandy Jacobs, Kevin McCollum, Jeffrey Seller, Wendy Orshan, Beth and Allan Williams, Nick Scandalios, James L. Nederlander, Paul Libin, Philip J. Smith, Robert E. Wankel, Jordan Roth, Daryl Roth and everyone else who has encouraged and supported me along the way.

I can only hope that I can inspire a few folks with my work in the same way that you all have inspired me.

A Personal Note From Ken

Individual Investors are the life blood of Broadway. Without you, there would be no *Chorus Line*, no *Rent*, no *Les Misérables,* and yep, no *Hamilton*.

Without you, there would be no Broadway as we know it.

As I said when I accepted the 2018 Tony Award for Best Revival of a Musical, *"*without the individual investors and Co-Producers who support Broadway shows, no one who works in the theater would have a job."

So, thank you for purchasing this book, for your interest in learning more about investing in Broadway shows and for supporting the art form that I love so much. It is because of you that Broadway and the theater will continue to be innovative, influential and inspirational, both now and for decades to come.

Best,

Ken Davenport
February 15, 2019

P.S. This is the very first edition of this book, which makes you quite the early adopter! Thank you! Since it's the first edition, there may be a few typos that snuck by my 142 proof readers before we went to print. We want to make sure we correct those for future readers, and you can help. Notice a typo or something that doesn't make sense, or simply have a question? Drop me a note at ken@theproducersperspective.com and help me make this book better for future readers. Thanks in advance!

Why I Wrote This Book

In 2011, I had a hunch. Based on the success of my blog, TheProducersPerspective.com, I had this feeling that there were thousands and thousands of people around the country and around the world who were interested in investing in Broadway shows.

I also had a feeling there were two major issues preventing these folks from investing:

1. They thought Broadway investing was only for the yacht-owning, Rolls-Royce driving, mega rich.
2. They didn't know who to talk to about investing.

I decided to test this theory when I produced the 2011 Broadway revival of *Godspell*.

Prior to this date, the majority of Broadway investing was done primarily by a small group of people and companies. New investors only got the opportunity to invest if they knew someone who knew someone who knew someone. Like many things in the theater industry, investing was a closed-door club.

Because *Godspell* was about "a community of people coming together," to quote its composer, Stephen Schwartz, I decided to put together the largest community of Investors and Producers ever. To do so, I announced publicly on my blog that instead of only taking investments from the usual suspects in amounts of $50,000 or more, I would accept investments from the public for as little as $1,000.

Sure enough, thousands of people from around the globe raised their hands, expressing interest in investing. Emails flooded my inbox and calls poured in. It took me days to get back to all of the interested parties.

When we completed our raise, over seven hundred individuals invested in *Godspell* in amounts from as little as the minimum of $1,000 to as much as $250,000. Many of these investors would never have invested in a Broadway show without that public announcement and the low threshold for entry. We successfully capitalized the show, enjoyed almost a year-long run, and my "crowdfunded" concept was the subject of a front page article in The New York Times. (See our online appendix referenced in the next chapter to read it.)

Since then, thanks to the success of shows like *Hamilton, Harry Potter, Wicked, Dear Evan Hansen*, as well as the popularity of all of the Disney properties around the globe, the nationally televised Broadway telecasts (*Sound of Music, Grease,* etc.), and more, the public's interest in investing in Broadway shows has only increased.

Through my blog, I used to receive one or two inquiries a month from people expressing interest in learning more about investment opportunities in my future shows. Now, it's not uncommon for me to receive several in one day.

As often happens when an industry experiences a gold rush like Broadway is experiencing now, new Investors rush in to the market in an attempt make a quick buck (the recent crypto currency craze is an example of this phenomenon). Unfortunately, jumping in to any industry without the proper education, understanding of the market, and without the right person to guide you can lead to very quick losses, especially in a high risk industry like Broadway.

That's why I wrote this book.

I wanted to make sure people like you, who are interested in investing in Broadway shows, are armed with the information needed to help you find the next big hit, but also to prevent you from making mistakes that could cause you to lose faith in investing in the theater. Because nothing pains me more than to hear about an investor who makes one investment in a Broadway show, hoping to find the next *Hamilton*, and makes a simple mistake that results in a loss, and never invests in a Broadway show again. (And usually, that one mistake could have been easily prevented by following some of the strategies I'm going to describe in this book.)

Broadway investing is a risky venture, without a doubt. But when done properly, with the right amount of due diligence, research, and advice (not to mention "a little bit of luck," to quote *My Fair Lady*), it can be a fun, educational, and yes, a very profitable experience. And if you learn the mechanics of investing in Broadway shows and follow the strategies I discuss in this book, I guarantee you will enjoy the experience much more *and* increase your odds of financial success.

So, let's get this show on the road.

The Structure of This Book

This book was written to give you a primer of the business model of Broadway, as well as to teach you the successful strategies I use to determine which Broadway shows I invest in and more importantly which shows I do NOT invest in.

At the end of each chapter, I've included a short quiz to ensure sure you have a general understanding of the previous chapter. Don't worry, there's no algebra in the quiz, but do be prepared to do some math! I believe it's important for all Investors to truly understand the concepts of investing, so do make sure you get all the questions right before advancing to the next chapter.

In addition to the material I've written for this book, I've also included several sample legal documents used for traditional Broadway investments as well as sample budgets, proprietary research, articles on investing, and more, all to help you become a smarter Broadway Investor.

Included in these materials are the results from the first and only demographic study of actual Broadway Investors, which I conducted in order to learn more about their experiences, expectations and results. (Within the book, I've included some statistics and actual quotes from this exclusive report to help you understand what it's like to be in an actual Investor's shoes . . . and wallet!)

Because these documents and reports are often quite large, we've put all of the materials online in an "online appendix" to save a few trees and to prevent those of you who bought a hard copy of this book from lugging around a three-hundred-page tome.

You can get all of the additional materials in this free online appendix at www.TheProducersPerspective.com/appendix. Much of the information is in the appendix, including the documents and budgets, has never been made publicly available so I know you'll find it very valuable. More importantly, I know it will help you in your search for successful and more enjoyable Broadway investments.

<u>Important Note</u>

In this book, we're going to delve deep into the logistics and nuances of the business of Broadway in order for you to make smart investment decisions to enhance your investing experience and hopefully add to your bank account as well.

That said, please let me first be very clear and state for the record that investing in Broadway shows is a *very* risky endeavor, not unlike investing in restaurants, race horses, venture capital, or other high risk enterprises.

While this book will teach you how to reduce that risk, there is always, <u>always</u> the chance that you could lose your entire investment . . . even if you have Hugh Jackman as your Star and Lin-Manuel Miranda as your Author!

That's why you should never invest capital that you can't afford to lose. Or as I say to all my first-time Investors, "You should write this check like you're never going to see it again."

And before making any investment, please speak to your investment advisor to make sure investing in Broadway is appropriate for your personal financial situation.

Or as my lawyers want me to say:

THIS BOOK IS FOR GENERAL INFORMATIONAL AND EDUCATIONAL PURPOSES ONLY. NOTHING IN THIS BOOK SHOULD BE CONSIDERED AN OFFER TO SELL OR A SOLICITATION OF AN OFFER TO BUY SHARES OR UNITS OF ANY ENTITY THAT IS DISCUSSED. FURTHER, NOTHING IN THIS BOOK SHOULD BE CONSIDERED AS FINANCIAL ADVICE IN REGARDS TO YOUR INVESTMENT DECISIONS. BEFORE CONSIDERING ANY INVESTMENT IN THE THEATER OR IN ANY INDUSTRY, WE STRONGLY ADVISE YOU SEEK THE ADVICE OF A FINANCIAL CONSULTANT, ATTORNEY, AND/OR ACCOUNTANT.

If losing an investment in a Broadway show would cause you to compromise your standard of living, then please stop reading and pick this back up when your economic situation changes.

But, if you have the appetite and the means to withstand the ups and downs of this industry and are still up for this fun and adventurous way to support the arts (and, yes, hopefully make a lot of money in the process), then play on, my friends.

Chapter One

Who Invests In Broadway And Why Should You?

One of the great myths of investing in Broadway shows is that it is only for those people who spend their weekends on yachts, fly their own planes, and who have personal masseurs . . . for their poodles.

And that's just not true. (Want to read the other myths of investing in Broadway? Visit www.TheProducersPerspective.com/appendix to read my list of the "10 Myths of Broadway Investing.")

While investing in Broadway shows does usually require an individual to have a certain net worth and disposable income, the barrier for entry is less than most people realize.

THE AVERAGE INVESMENT IN A BROADWAY SHOW

As a Broadway Producer, I travel all over the world and talk to a lot of people. When the subject of what I do comes up, the conversation often leads to the business model of Broadway and how shows are funded. When I explain that most shows are typically funded by small investors, just like any startup company, the person I'm talking to will often ask, "What's the minimum investment required?"

And I don't answer.

Instead, I treat the conversation like my own mini-focus group and ask the same question back to the person asking the question. "What do YOU think the average investment is? Go ahead. Guess."

Before I continue . . . pretend you and I meet while in the American Airlines lounge at JFK and I ask YOU . . . "What do you think the average investment in a Broadway show is?"

What would you say?

Go ahead. Think about it. Write it down. It's ok. I'll wait.

Got it? Good. What did you guess?

When I've asked this question of people around the world, the answers always shock me. I've heard everything from $100,000 to $250,000, and even more! The fact is, **the average Broadway investment is around $25,000**. And it's sometimes possible to be able to invest for as little as $12,500 or even $10,000, especially if you are just starting out, and if you meet the right Producer. And if you're interested in Off Broadway shows, the number can be even lower, since the amount the Producer is raising is lower and the risk higher.

Did you guess more than $25,000? If you did, you've got a lot in common with most people new to the industry. Just remember, investing in Broadway shows is more accessible than most people think.

WHO ARE THE INVESTORS ON BROADWAY?

As I stated above, the idea that Broadway investors are only socialites who sit on beaches all day and discuss where they're going to "summer" is just not true. And no, the cliché of the "Little Old Ladies" from *The Producers* isn't true either.

Broadway Investors come from all walks of life, and every profession you can imagine. Broadway Investors are accountants, lawyers, real estate developers, pharmacists, authors, actors, CEOs, doctors, and more.

Personally, I've had just about every profession you can imagine invest with me. (In fact, my investors are from such a diverse group of vocations that we have networking events for my investors so they can help each other grow their own businesses.)

Here is some hard data from our Broadway Investor survey which confirms the demographics of the Broadway Investor:

<u>Gender:</u>
Male – 64.8%
Female – 35.2%

<u>Age:</u>
18-24 – 3.1%
25-34 – 10.3%
35-44 – 17.3%
45-54 – 30.8%
55-64 – 27.8%
65-74 – 8.9%
75+ – 1.8%

<u>Job Field:</u>
Accounting/Finance – 11.7%
Advertising/Marketing – 5.4%
Arts/Entertainment – 34.4%
Education – 5.4%
Engineering – 1.3%
Environment and Natural Resources – 0.7%
Food/Culinary – 1.3%
Government/Politics – 1.0%
Health Care/Medicine – 5.0%
Human Resources – 1.7%
Insurance – 1.0%
Journalism – 2.0%

Law/Criminal Justice – 5.7%
Psychology/Social Work – 0.0%
Real Estate – 2.0%
Retail – 0.7%
Sales – 1.7%
Sciences – 1.3%
Sports – 0.3%
Technology – 2.7%
Tourism/Hospitality – 0.3%
Travel – 0.7%
Visual Art/Design – 1.0%

For the full results of this survey, including state of residence, income levels and more, visit www.TheProducersPerspective.com/appendix.

WHY DO INVESTORS INVEST?

The one characteristic that all Broadway Investors have in common is their love of the theater. Investing in the theater is a form of "passion investing," similar to investing in fine art, restaurants, or thoroughbred horses – or any venture that may bring joy or a thrill to an investor but also has potential economic upside. Passion investing provides the potential for two types of ROI ("Return on Investment"): financial and emotional. It's why so many investors invest again and again, even when they've incurred losses . . . because they love the theater.

I'd bet that one of the reasons you picked up this book is because you're passionate about the theater, or have someone very close to you who is. The love of the art form is usually what brings people to our investing table.

But there are many other reasons why Investors choose to invest in the theater. Here are a few:

SUPPORTING THE ARTS

Getting a show on Broadway is like getting a piece of art put on display at the Metropolitan Museum of Modern Art! That show, just like the piece of art, will be seen and studied and its value will increase, because there is no greater stage for a play or a musical than Broadway.

It's true!

New York City is the theatrical capital of the world (I don't care what London says) and shows that happen on our Broadway stages have a ripple effect throughout the rest of the world.

The theater industry is similar to the fashion industry in that respect. When a new clothing line debuts in Milan or Venice, buyers from all over the world will flock to the unveiling and purchase the new styles to bring back to their own shores (or knock them off). The same is true for the theater. The theater is a commodity. Every year, theater buyers from all over the world come to Broadway to see the new crop of shows in order to decide what they will produce or present in their "hometown," whether that's a casino in Macau, a community theater in Muskogee or a high school in Miami.

When a show is produced in theaters like these in locations all over the world, the show's message is heard by more people, which means that message can inspire, entertain, educate and yes, even change people's lives.

Because of that, the theater is a vital part of our society and an essential art form. As legendary businessman Victor Pinchuk said, "Art will change society faster than politics."

In this age of new technology, with entertainment available on laptops and smart phones and watches (!), those who invest in the theater help ensure that the theater will survive over the next hundred years and continue its grand tradition of shaping our society.

TAX ADVANTAGES

Many successful people of all forms choose to support the arts by donating to non-profits, because in addition to supporting the arts, the donor receives a deduction on their taxes for supporting a charity.

There are tax advantages to investing in Broadway shows as well, *and* there is always the chance that those investments may make money. That's something that can never happen when you write a check to a non-profit.

An investment in the theater is just like an investment in any for-profit company that seeks investment. At the end of each year in which your investment is active and the company has not been closed (and in this case, "closed" doesn't mean end its run on Broadway, but rather when the legal entity has been shut down and all activity has ceased), you will receive a "K1 Tax Form" from the entity, just like you would receive for any other investment you make. This form which list the profit or loss attributed to you.

If the show has lost money, you will be able to write off that loss on your tax return, as you would for other investments. So, a loss in a commercial investment can decrease your tax liability just like donating to a non-profit. The major difference between the two is that you cannot choose exactly when that loss will occur. When you donate money to a non-profit, you can immediately write that donation off on that year's tax returns. This is why so many non-profits hit you up for donations in December! They know that individuals are doing their tax planning before the end of the year, and that many people would rather donate money to charity than pay taxes on it.

Of course, if a show you invested in is profitable, then you will owe taxes on that profit. But I've never gotten a complaint from someone who has to pay taxes because a show they've invested in has made them money!

(GOOD NEWS! One tax complication of years past was finally corrected very recently. On some profitable shows, Investors used to receive tax bills on profits that they had not yet received, also known as "phantom income." After some successful lobbying on behalf of the Broadway industry by our trade association, The Broadway League, that situation has been resolved. To read more on this subject, please visit www.TheProducersPerspective.com/appendix for a white paper written by one of Broadway's top accountants (and mine), Robert Fried of Withum.)

EDUCATION

Many of my Investors invest in the theater to learn more about the business of Broadway. Some want to produce themselves, either as a Co-Producer (see Chapter 7 on "Advanced Strategies") or as a Lead Producer. This was one of the reasons I started looking at investment opportunities years before I produced my first show.

Some of my Investors are writers who want to understand how the business works on the "other side of the table." Others are looking for a career in arts management or administration. Some have a fascination about how things work and want to invest not only to support their hobby, but also as a way to learn the business of "the business."

Of course, there is no better way to learn than by doing. If you study real estate investing or stock market investing or even want to be a better poker player, the gurus of those worlds will tell you that the best way to learn the "how to" is to get in the game and make your first investment, even if it's a small one. There is no better education that actual participation.

In fact, I talk to a lot of young people who want to be Producers who ask me if they should go to graduate school to get a Master's Degree in theater or arts administration. Don't tell this to any of the graduate schools out there, but I've been known to tell them to forego graduate school and take the money they were going to spend on that (overpriced) education and invest it in several shows instead. I'd rather they buy a seat at a Producer's table where they can learn, network . . . and possibly even make money.

NETWORKING

The people who invest in and produce Broadway shows include some of the most successful people in their chosen field. By nature, investing in the theater has a high "admission fee," which means that the people involved are likely to have achieved a certain level of financial success or are of a certain net worth. When you invest in the theater, you'll immediately be admitted to this club, which includes top real estate agents, psychiatrists, matrimonial attorneys, and surgeons, not to mention folks on the Forbes lists, hedge fund managers, politicians, and many more. I often say that the opening night party of a Broadway show is the most diverse gathering of successful people in New York City, but all with one thing in common . . . their love of the theater! Or as the infamous gossip columnist for the NY Post, Cindy Adams, once said, "Big names. Broadway. New York. Opening night. Nothing more thrilling. Where else would anyone want to be?"

Many Investors will invest in the theater as a way to network with this influential group, not unlike joining a golf club or attending a conference What's a $25,000 investment if you can meet the right client for your real estate business, law practice, or . . . maybe you're raising money yourself for your own high risk industry? Maybe you're even raising money for your own show! I've known several Investors who have made money by investing in shows just by the business they've picked up while doing it.

I was at a business lecture when I first heard the following quote which has changed my life in many ways. "What you're not getting from the world, you're not giving to the world." So, if you're looking for investors, you might try starting to invest yourself.

INVESTING FOR THE WHOLE FAMILY

In addition to networking to help yourself or your own business, investing can also have the benefit of helping those closest to you.

One of the newest classes of Broadway Investors is parents of children who are pursuing a career in the arts. By investing, parents can learn the ins-and-outs of the business their child is about to devote his or her life to, and they are also able to make strong networking connections within the business. At opening night parties, parents can introduce their children to Agents, Directors, Casting Directors, and more.

People sometimes think that because success in the theater is dependent upon a certain amount of talent that the old expression, "It's all about who you know," doesn't apply. Well, it's actually the opposite. It applies even more! Because of the competition within the industry in every profession from Acting to Stage Management to Producing, it's often more important to have the right connection to get a foot in the door in order to be considered for a position, *no matter how talented you are.*

Please don't think that I'm suggesting that there is an easy way to buy your child or relative's way into the business. In fact, if you suggested such a thing to most Producers, they might be turned off by the question. But it is possible and common for Investors to get auditions, internships, and interviews for people close to them in exchange for an Investment, so don't be afraid to ask. In other words, investing can get someone in the room. And then it's up to the person in that room to deliver. But sometimes, just being around the industry can get you in the industry.

This trend of "Family Investing" has been featured in articles in Barron's and in The New York Times, both of which can be found in our online appendix at www.TheProducersPerspective.com/appendix.

GOOD OL' FASHIONED FUN

If you're currently investing or considering investing in other forms of alternative investments, I challenge you to find one that is as fun as investing in Broadway.

I always say to my investors that while I can't guarantee a profit, I can guarantee you an experience unlike any other. (P.S. No one can guarantee a profit, in any industry, including the stock market.)
When you invest in a Broadway show, you have the opportunity attend exclusive events (like the opening night performance and party), meet celebrities, participate in marketing discussions about that show, see closed-to-the-public rehearsals and much more.

And there's nothing like seeing a show performed and watching the audience respond to something you helped make happen. It's why when I attend my shows, I usually watch the audience instead of the performers on stage. Seeing an audience laugh, cry or give the performers a standing ovation for something you helped produce is a thrill like no other.

For those with the capital to risk and the love of theater to go along with it, investing in the theater is a much more interesting and entertaining way to invest than a hedge fund, real estate investment trust, or an internet startup. Not that you should stop investing in hedge funds or the like, but if you have the assets for those types of investments and love the theater, there's no reason not to add Broadway investments to your diversified alternative asset portfolio.

PROFIT

I've saved the best for last.

Many investors *do* invest in Broadway shows with the goal of turning a profit and making money.

Of course, many people who aren't familiar with how Broadway works think it's impossible to make money on Broadway. When I mentioned the idea to one gentleman while I was on a golf course, he laughed and said, "Investing in Broadway is like putting a match to your money."

But that's just not true. Is it easy to make money on Broadway? No. Is it risky? You betcha. But as you'll see in subsequent chapters, investing in Broadway is often less risky than other alternative investments, *and* after you finish this book, you will be armed with systems and strategies to help reduce that risk.

(The irony is that the gentleman above had invested in three startups that all went belly-up!)

Still don't believe me that Broadway can be a place to make money? Consider this simple fact.

While all of the reasons that we've discussed in the last few pages are very valid reasons for investing in a Broadway show, if there was *not* a way to make money, and if money wasn't being made on a consistent basis, *eventually investors would stop investing.*

But they are not. In fact, there are more Investors investing in Broadway than ever before. And there are more Broadway shows and more people attending those shows than ever before. In 2018, Broadway grossed over $1.8 billion dollars, an increase of $400 million from only two years prior.

Twenty to thirty years ago, you could walk up the streets of Times Square and see many "dark" (empty) theaters. Not anymore. Not only are the majority of our theaters filled all year long, but I was recently told by an executive at one of the companies that own a number of Broadway theaters that over thirty shows (!) were waiting for theaters for the upcoming Broadway season. That means that there are more investors lining up as well, eager to find the next bit hit.

Why are they lining up?

Because it *is* possible to make money. If it wasn't, no one would do it.

In fact, not only would Investors stop investing if there wasn't the potential to turn a profit, but Broadway shows would no longer be produced commercially. Instead, Broadway would become a museum and would be funded only by grants and donations (no unlike the Opera). And while several non-profit theater companies do produce on Broadway, the majority of Broadway productions are produced by for-profit or commercial companies. Why? Because the Producers know there is money to be made. And a lot of it.

TAKE IT FROM DISNEY AND UNIVERSAL

You're probably aware of Disney's success in movies, right? Just through their recent acquisition of Lucasfilm alone, the company has earned more than $3 billion for its first three *Star Wars* films: *The Force Awakens, Rogue One*, and *The Last Jedi*.

However, get this . . . the stage production of *The Lion King*, which opened on Broadway in 1997, has generated more than $8 billion in global box office from productions and tours. That makes *The Lion King* musical the highest-grossing entertainment property in history.

Need more proof that a lot of money can be made on Broadway?

In its first ten years, *Wicked* grossed $3 billion from productions in New York and other cities around the world, putting it on track to become the most profitable entertainment property in the 100-plus year history of Universal Studios, *Wicked's* majority investor. That means *Wicked* will make more money for Universal than blockbusters like *Jurassic Park* and *E.T.*

Now, obviously shows like *The Lion King, The Phantom of the Opera, Les Misérables, Hamilton, Wicked*, etc. don't come along every day. They are the outliers.

But they do happen. And more often than you'd think. In the past five years alone, Broadway has produced several mega-hits that could have ten-plus year runs both on Broadway, on tour and around the world.

When you're finished with this book, you'll have a better chance of recognizing one of these potential mega-hits, and you'll be armed with the information and contacts you need to invest in it!

WARNING! Despite my enthusiasm and optimism that there is a *Hamilton* out there waiting for all of us, please don't expect that you're going to find one of these Broadway juggernauts with your first investment. (I often say to my first time investors, "I believe I will have a *Wicked* or a *Hamilton* someday . . . I just can't tell you exactly when that will be!") While it can happen quickly (I have a friend who stumbled into a *Wicked* investment having never invested before, and another who threw a little money into a little show called *Jersey Boys* his first time out), I think of investing in Broadway shows like drilling for oil. You have to drill a lot of holes before you find a gusher. But when you find one, that oil well will usually pay for any of the other holes you drilled that didn't produce a drop, while that gusher can keep pumping for years. (*The Phantom of the Opera* investors and in some cases their children (!) are still getting checks thirty years later, and probably will for years to come.

According to an article in *Forbes*, investing in Broadway, "represents the best outcome of a low-cost, high-yield investment . . . The immediate profit margin is slim at first; there are only so many seats in a single theater. But unlike films, musicals can run at capacity for years (or decades). You're not going to turn a profit overnight, but you're looking at a very, very long green tail."
And for anyone thinking Broadway attracts a niche audience, more than fourteen million people saw Broadway shows in 2018 (another record), which is more than the number of people who attended all ten professional sports teams in both New York and New Jersey during a single year.

If you are able to find a show that appeals to a large percentage of those theatergoers, you'll be telling everyone you know that yes, money, and a lot of it, can be made on Broadway.

HEAR "WHY" FROM ACTUAL INVESTORS

A few years ago, I surveyed several hundred Broadway Investors for my blog, TheProducersPerspective.com, in order to determine what their experiences were like, and discuss some of the questions that we've asked in this chapter including: who they are, why they invested and what they were looking for when investing in a Broadway show.

Here are a few answers to the question, "Why do you invest in Broadway?"

Investor #1, Capital Investor, in his fifties: "I feel like I'm making a contribution, which makes me feel good irrespective of the outcome. It's also fun to go to the opening party of a show that I have helped create in a small way."

Investor #2, attorney in his fifties: "There are five reasons: Diversification. It's fun. Unlike many other investments, I get to see the product before I invest. There's a potential to make a great deal of money. And there is also a potential to make money post-Broadway run either on tour, at other locations, or overseas."

Investor #3, tech entrepreneur in his sixties**: "**For two reasons. First, to support and influence the future of great theater on Broadway and beyond. Second, to have a very different and unique experience and relationship to the world of acting, production, music, and theater. Being a producer and investor has changed us, by broadening our view of excellence, extending our sense of what moves and motivates people, and stretching our sense of risk-taking as a key element in changing the world."

Investor #4, attorney in his fifties: "Because it has always been a great passion of mine, I want to see it thrive, and I am such an optimist that I am eternally hopeful that I will make a little money with it. I also invest because I am at a place in my life where I can afford to in some small way, and the theater needs people to invest to keep it alive."

Investor #5, medical technology professional in her fifties**: "**I invest because it reflects my passion for the theatre. I get to learn about the world of Broadway producing, and it exposes me to all that happens to bring a show to stage. And it fits into my mixed portfolio of investments strategy, Broadway being the higher-risk aspect."

Investor #6, analyst in his thirties: "I love the theater and enjoy supporting it. I'd also like to think that I'm better at picking successful shows than others are although I know that's not the case. I also want to make a return on my investment."

Investor #7, TV program developer in his forties: "I have worked in the entertainment industry for many years, and even though it has been mostly in TV, I have the greatest passion and appreciation for (good) theater."

Investor #8, small business owner in his fifties: "Simply put, because I love it. The opportunity to participate in the mounting of a production that might deliver entertainment, add to the public conversation on a topic, or possibly change the course of someone's life—as it did for me many years ago—are all motivating factors each time I invest. I was an avid Broadway fan for years before I was in a position to invest, and I looked forward to being even a small part of the process."

Investor #9, mother in her forties: "I invest in the theatre because it's fun. The experience that the project generates is as important to me as the financial return. We all have many options and opportunities to invest money in places that don't produce an experience and most of those investments are far less risky than Broadway. I need to believe in either the project I chose or the people I choose to invest with. Typically, both.

I've made the mistake of investing solely based on the project, and I will not do that again. If there isn't a personal connection to the lead producer or someone on the creative team, I don't want to be involved. I want to know that I will be part of the inside track. Maybe that just means getting emails and updates on the progress, but I want to feel like my money actually matters, whether they think it did or not. The times I have invested and received nothing more than a “thank you for your check” have left a bad taste in my mouth and have definitely shaped the decisions I will make in the future with regard to investing. The people I’ve met, the friendships, relationships, and bonds that have been created are invaluable to me, and something that will keep me coming back for a long time, too, I suspect. Celebrating opening nights and other events with these people make the experience that much more enjoyable.”

***Investor #10, CFO at arts organization in her fifties*: “**I have loved live theater since I was a child and now have the money not only to see theater but to help others to see it too by investing.”

Investor #11, accountant in his forties: “I invest in theater because I want to be a part of theatre. A long time ago I decided that my profession would be accounting. No regrets. It may have precluded me from gracing the stage any longer, but it turns out that now I can afford to see all the shows I want—in the last twelve years I have seen over seven hundred Broadway and off-Broadway productions—and I can now afford to be a part of paying the salaries and building the sets for all those people who made the choice to live their lives in the theatre. Of course, buying a ticket to see a show in itself also goes in a small way towards that end, but investing some of your own capital in a larger way makes it all much more rewarding no matter whether you profit or not. Knowing that I am helping, albeit in my small way, to support art and artists makes it all worthwhile. Earning a profit would just make it that much sweeter and maybe let me invest that much more the next time.”

QUIZ!

1. Which one of these is a reason for someone NOT to invest in the theater?
    a. They love the theater.
    b. They want to learn more about producing.
    c. They don't like risky investments.
    d. They hope to earn a profit.
    e. None of the above.
2. What show did Universal announce would be more profitable than *Jurrasic Park*, & *ET*? (no space between these first 2 questions)
    a. Billy Elliot
    b. Moose Murders
    c. ET The Musical
    d. Wicked
    e. The Lion King
3. Generally speaking, if you lose money on a Broadway Investment, can it be used as a deduction on your tax return?
    a. Yes
    b. No
    c. Only if the production is 501(c3) Non Profit
    d. Off Broadway, yes. On Broadway, no.
    e. Depends on when the show closes.

ANSWERS: 1(c), 2(d), 3(a) but make sure you check with your accountant before making any investment decisions to determine exactly how it will affect your taxes!

Chapter Two

The Risks of Investing in Broadway

If this book had a soundtrack, you would have heard ominous chords played on a *Phantom of the Opera*-like organ right after you read the title of this chapter.

Spoiler alert: Investing in Broadway shows is risky.

Are you shocked?

I didn't think so.

Because if you bought this book, then I'd bet you the cost of it that you already knew investing in a Broadway show was a high risk proposition. But you bought it anyway, because you know, like I do, that getting involved with anything requires more than just knowing if that activity is risky or not. Because, frankly, every activity, from investing in the stock market to walking down the street, is risky.

You know that before you decide to get involved in any investment opportunity, you must ask yourself three things:

1) How do we measure the risk compared to other opportunities we are involved in or may want to be involved in?

2) Are there other unquantifiable or non-financial ways to get a return on the investment?

3) Are there strategies that we can learn to help decrease the risk?

The answer to all three of these questions when referring to Broadway Investing is, of course, a resounding "yes," and that's what we're going to spend the rest of this book discussing.

You see, every investment opportunity, from blue chip stocks to hedge funds to real estate, carries risk. The moment someone offers you an opportunity in an investment of any kind, theatrical or otherwise, that has ZERO risk . . . well, to quote Jenny from *Forrest Gump* . . . “Run, Forrest! RUN!”

All investment opportunities have risk. Period.

Therefore, the question to ask yourself when considering an investment opportunity is not, “Is this risky,” but rather, **“How risky is this?”** When you can properly evaluate the risk of an opportunity only then can you decide whether or not you are willing to take that risk. Since every individual’s situation and risk profile is different, there is never a simple *invest* or *don’t invest* formula or algorithm.

In subsequent chapters, I’m going to walk you through the due diligence process I use to make my investment decisions and how I recommend you make yours. This process begins with an assessment of the amount of risk. Once I determine that risk, only then can I decide whether I have the appetite for that amount of risk *at the time that I’m making the investment*.

For example, I find that investors are much more willing to take a risk *after* their kids graduate college. Makes sense, right? That’s why there is no simple yes or no program that can tell an Investor when to invest in a show or not. <u>When you are evaluating a potential investment, you must make your own decision based on your current situation and the risk of that specific production.</u>

AVERAGE SUCCESS RATES ON BROADWAY

Before we start evaluating individual opportunities, let's look at the risks of the entire industry in terms of how many productions succeed or not.

When I run into people who say, "Oh, I'd never invest in Broadway because it's too risky." I usually quickly follow up with, "Do you know the average of how many shows on Broadway make money?" They can never answer that question. Not too many people outside our industry can! Ironically, they've chosen the *dramatic* answer that Broadway investing is just too crazy of an idea, instead of learning the actual facts and figures

But not you.

We're going to put those "Broadway investing is like putting a match to your money" generalizations and clichés aside and arm you with the information you need to determine how risky the industry is.

While Broadway doesn't officially publish when a show reaches profitability or "recoups" (short for "recoupment," or also known as "getting in the black"), the generally accepted Broadway statistic is that <u>one out of every five (20%) of Broadway shows recoup its investment.</u>

All of a sudden, Broadway investing feels different, right? Because we now have an approximate gauge of the overall success rates in the industry, which allows you to immediately assign some degree of risk to a possible investment when applied to your personal situation.

Interestingly enough, in their terrific book *Stage Money*: The Business of The Professional Theater, by Tim Donahue and Jim Patterson about the economics of Broadway, the Authors reported that during the Broadway seasons from 1999–2007, approximately one out of three shows (about 33%) recouped their investment.

That may be a bit too narrow of a window to study in order to draw a definitive conclusion about recoupment rates, and therefore I believe that this figure is a bit too optimistic to use when calculating overall risk of the industry. My office studied recoupment rates over a twenty-year period and came to the conclusion that the 20% number is more accurate over the long term. (Because of inflation, to go back further back than twenty years would include shows with much lower costs and different economic models, which would skew the data. To see my complete report on recoupment rates and the common characteristics of successful shows visit www.TheProducersPerspective.com/appendix).

I suspect that if we actually had the recoupment stats of every single show that has played Broadway in the last fifty years or so, it would end up somewhere between the generally accepted 20% and the 33% figure, or closer to 25% (or one out of four).

But for the purposes of this book, and in order to keep our estimates conservative, we'll use the generally accepted 20% as the average number of commercial shows that recoup their investment.

If you accept this data, and you should, you now know that investing in Broadway shows isn't putting a "match to your money." Yes, it's a risky investment but investing in Broadway shows leads to profit approximately 20% of the time on average.

WHAT ABOUT THE OTHER FOUR SHOWS?

Another one of the great myths of investing in Broadway shows isn't about the shows that make money, but rather the shows that don't make money.

When potential investors hear the "1 out of 5 shows recoup" statistic they often *mistakenly* believe that the other four shows result in complete losses that don't return a penny. They believe that either you make a lot of money, or you lose all of it.

While it is possible that you can lose your entire investment, that doesn't mean you will. Just like a stock that falls precipitously from where an investor might have bought it, it rarely goes down to zero, and is usually always worth something, even if that's lower than the purchase price.

A show that doesn't make money could still return 10%, 50% or even 90% of your investment and still be considered one of the "Other Four Shows" that don't recoup. While no one wants to lose money, wouldn't you agree that there is a big difference between recouping 50% of your investment and getting nothing back? This is often when the non-financial returns or "perks" help satisfy Investors. Because, for many, if they get a certain percentage back from the original investment, and also get access to opening night, educational opportunities, etc., then they are more satisfied than had they only received the limited financial return. (I often hear Investors saying, "If I can get 50% of my money back, I'll be happy.")

That said, because Broadway investing is a high-risk endeavor, let me again be very clear and state that there is always a possibility that you will lose your entire investment. In fact, I always tell my first-time Investors to assume the worst case scenario when making an investment, in order to manage their expectations. I often say, "Write this check like you're never going to see it again." When you understand and accept what could happen, even if it's the absolute worst case, you'll end up enjoying the experience that much better. This also helps potential Investors understand that they should not invest capital that they need to maintain their current standard of living.

YOU COULD LOSE IT ALL, BUT COULD YOU LOSE MORE?

Another common concern among first time Investors is that they can lose MORE money than they invest. This is another misconception. You cannot lose more than you invest. Any operating agreement for a

Broadway production that crosses your desk most likely includes language similar to the following:

> No Member shall be personally liable for any debts, obligations or loss of the Company in any event, except from the capital contributed by him or her hereunder.

And . . .

There shall be no overcall.

This language protects you by making it clear that Broadway Investors are only liable for the amount that they invest and no more, regardless of what happens with the production.

> TIP! When investing, ask your Producer to point out the language that "limits your liability" to only your investment.

If the show ever needed additional funds to keep running and the Lead Producer decides that it is in the show's best interest to obtain those funds, it would be his or her responsibility to raise or invest the additional money. This is called a "Priority Loan," and is discussed in greater detail in Chapter 7, "Advanced Strategies." The important thing for you to remember is that if a Producer asks you for an additional investment beyond your original amount, this additional investment is optional, provided you have language similar to the above in your agreement.

HOW DO OUR SUCCESS RATES COMPARE TO OTHER INDUSTRIES?

The average chance of a show's financial success is only one part of determining the general risks of investing in Broadway shows. In order to really understand how risky investing in the theater is, we need to compare it to investing in similar opportunities in different industries.

First, it's essential that all Investors understand that Broadway shows are like startup companies. An investment in a new Broadway show, especially one that is original and has no previous brand recognition (e.g. *Dear Evan Hansen, A Chorus Line,* etc.) is like investing in Uber before it became Uber, or Facebook when it was just a website catering to college kids. You're investing in a brand new company with the hope that it will one day become a household name and global success.

In fact, as a Broadway Producer, I call myself a "Serial Startup Guy," because every new show requires new Investors, a new marketing plan, a new management structure or creative team, etc. While sure, there are some "blueprints" to follow when producing a show, and many of my Investors do invest in all of my productions, you are still creating and launching a brand new product that has never been seen before. That process is similar to launching any new product in any industry, whether it's a soft drink or a ride-sharing app. That's why all startups are inherently risky but can be much more profitable than investing in existing companies because you are getting in on the ground floor.

But how risky are Broadway "startups" compared to other startup companies? That's the question we must answer in order to ascertain the risks of Broadway investing.

Ok, quiz time . . . what do YOU think is the average success rate of all non-Broadway startups in this country?

If Broadway shows reach profitability 20% of the time, would you guess 40% of other startups are successful? 30%? Certainly, they have to be less risky than Broadway startups, right?

Well, according to a 2015 article in *Forbes,* the success rate of any startup is only 10%.

Instantly we have a comparative figure to help us gauge the risk of investing in Broadway shows. (And all of a sudden it doesn't look as risky as other forms of investing, now does it?)

Broadway shows are risky (getting tired of me saying that yet?) but I'd argue that many are *less* risky than venture capital, private equity, hedge funds, or some other alternative investment opportunities.

Many Investors don't think twice about venture capital, or other similar high-risk vehicles but shy away from Broadway because they consider it too risky. Or get this . . . I met a potential investor recently who was nervous about investing in Broadway. During our discussions, he admitted that he invested six figures in Bitcoin! (I often ask my potential Investors what other high-risk ventures they've invested in, because it helps me determine their appetite for risk. In many cases it reminds them that they can tolerate more risk than they think. If they've invested in Bitcoin, then a Broadway show certainly fits in their alternative investment profile, they usually just need to understand how it works.)

Broadway is risky (yep, I said it again), but that risk can be mitigated as you'll see in future chapters. And because of its explosive growth potential and long-term high profit margin (remember Disney and *The Lion King,* or Universal Pictures and *Wicked*), it's an asset class that most people of a certain net worth should consider if they are considering other alternative investments.

HOW MUCH CAN I MAKE?

Did your mouth start watering when you read the above? It's ok. Mine did.

The worst-case scenario when investing in Broadway is losing your original investment. Once you accept the financial downside of Broadway investing (or any investing), you must also understand how much you can earn if a show is successful.

The upside of Broadway investing is a very important factor to consider when making an investment, because the potential profit on an investment helps determine how risky it is. Simply stated, when there is the possibility for a very large payoff for a low investment, it actually *lowers* the risk. (If you're a poker player, this concept is similar to "pot odds," which is how players calculate whether or not it's worth "calling" certain bets . . . because if there's enough money in the pot, they go for it, even if it seems like a long shot!)

For example, have you ever played the lottery? Most people have, whether on a weekly basis (I have a subscription) or only when that Powerball reaches a certain threshold, like $500 million. The odds are like a billion to won that you'll actually win, but you do it anyway, because the investment ($1 or so) is so low in relation to the potential payout.
This same theory is used to calculate risk in everything from stocks, to horses and yes should be considered when making Broadway investments as well. At times, Investors will choose to bet on an option with "longer odds" simply because if it does hit, the payoff will be much better than other investment options. (I opted to produce *Kinky Boots* in 2012 even though we were a long shot to defeat *Matilda* for the Tony Award for Best Musical. I knew that if we were able to win (and I was very confident we would), that my investors would earn more money than had we invested in a show with less risk. That gamble paid off!)

GET TO THE RETURNS, KEN!

What most people don't realize is that there is more than one way for a Broadway show to earn money for its investors.

The most direct and biggest payoff Investors receive when investing in a Broadway show is when that show recoups its original capitalization and pays profit to Investors. How much profit a show pays depends on a number of factors, including the operating expenses, grosses, length of run, etc.

But, and here it comes, it is not uncommon for Broadway's biggest hits to pay back its investors 10% or more in profit . . . *per month!* That's right, if you invest in a show that turns into one of our "oil wells," you can double your money every single year . . . for many years.

Recently, some shows have paid even more than 10% profit per month, with one show paying investors as much as 25% in profit in one month.

Again, and I can't say this enough, these types of returns are the outliers and examples of the BEST case scenario on Broadway. But I believe it's important for you to know the *potential* returns when valuing an investment opportunity, and also to know that these kinds of returns do happen, no matter how rare. If you are going to acknowledge the downside, then you also must acknowledge the upside, even if that upside is harder to obtain. When investing, the important thing to do is not expect these kinds of returns, since they depend on a variety of factors, some of which are beyond your control.

But as my shrink likes to say, "It's ok to fantasize, as long as you are ok if that fantasy doesn't come true."

(In a future chapter, I'm going to teach you tips on how to help you find a big hit, based on studies we've done of the similarities of the most financially rewarding shows in history.)

OTHER WAYS BROADWAY SHOWS PAY BACK THEIR INVESTORS

For a successful Broadway show, New York is just the beginning. Remember how I said Broadway shows were like startup companies? Well, when you invest in a startup, you're hoping that startup goes global. And the same is true for a Broadway show.

If a show is successful on Broadway (and sometimes when a show isn't successful), that show can tour the United States (sometimes for multiple years) or can be mounted in Toronto, Australia, London, and in cities all over the globe.

While each of these additional companies will be structured as a new company (another LLC or LP), as an investor in the Broadway company you'll traditionally be offered the opportunity to invest in those additional companies. This "right of first refusal" is usually spelled out in your investment documents.

TIP! Make sure your investment documents give you the right to invest in additional companies.

Additional companies of successful shows are often much less risky than the original production, because you already know how the market responded to the production, and because the brand of the show has been established. You may have great reviews, Tony Awards, and more.

National Tours are one of the least risky forms of producing when they use a "guarantee" model. In this scenario, the economic model is the exact opposite of the Broadway production, where Investors assume all of the risk. On Broadway, the Producer rents the theater, pays all of the expenses and hopes enough people buy tickets every week in order to meet those expenses and pay back the capitalization.

Under a "guarantee" touring model, a Producer is paid a fee for delivering the production to each specific city and therefore can budget how much income he or she would have over the life of the tour (e.g. a guarantee of $300,000/week over 30 weeks would been a base income of $9,000,000). With that figure in hand, the Producer can budget a show that is profitable on paper before rehearsals even begin. When you can "back into a budget," as I call this process, the risk is very low for an Investor, since the bulk of the risk is on the Presenter of the show in each market (the local Producer) who "guarantees" the fee to the Producer.

This is when things get exciting for Investors. If the Broadway show is successful and is paying profit, and subsequently, a national tour is launched, which also pays profit, the Investor has parlayed their original investment into two "hits." And the second came with much, much less risk.

And when shows are extremely successful, they can quickly spawn multiple productions and quickly! For example, I have several friends who are not investors in one production of *Hamilton.* They are investors in FOUR productions of *Hamilton*. When you have multiple productions paying profit, it's easy to see how the returns can add up.

But even if you don't invest in the additional companies, those additional companies will usually pay a royalty or a portion of profits back to the "Mother Company" or original Broadway production, so you will still receive a passive benefit from these companies.

TRICKLE DOWN RETURNS

Investors who are new to the industry often believe that financial returns end when the show they've invested in "closes" (stops performing) on Broadway.

In reality, not only do successful shows spawn national tours and additional companies all over the world, but eventually, these shows will be licensed to regional theaters, summer stock theaters, community theaters and even high schools.

These theaters, including those high schools, will be obligated to pay a royalty to the Authors of the show. And for a number of years after the close of the Broadway production (usually somewhere between seven and thirty years subject to the Broadway production's agreement with the Authors), a portion of that royalty goes back to the show's original Investors. That's right, if you're an Investor in a Broadway musical, you could earn money from the Eastern Sheboygan High School Drama Club's production of that musical years after the Broadway production has closed.

This type of revenue is called "subsidiary rights income" and doesn't just include other theatrical productions. If you invest in a musical or play and that show is made into a film or a TV show etc., then you may benefit economically as well. Most additional use of the material or adaptation of the material will result in additional subsidiary income for the investors.

A production with potential in the subsidiary market is another great way to mitigate risk, as I'll demonstrate in a later chapter. Shows that appeal to other markets (especially high schools) can generate a great deal of post-Broadway revenue, *regardless of their success on Broadway*, and are therefore less risky than shows without high subsidiary rights value. One of the most produced plays in the United States is a play that you've probably never heard of, *Almost Maine.* This play had a very short run when it was produced Off Broadway, but it found a life in the subsidiary market and has generated a great deal of revenue well beyond its original production.

TIP! Want to know what shows get produced the most at high schools and many community theaters around the country? Shows that have big casts, since both of those types of organizations like to involve as many people as possible in their productions. In high schools, shows with female leads often are produced more frequently, since there are usually more female performers than male in the local talent pools. So, if a show you're considering has a big cast and a female lead, you may have a highly licensable property!

Remember, there are over 25,000 public high schools in this country and over 10,000 private high schools and most have drama departments. That's a lot of high school plays and musicals, which means a lot of potential royalty income. While these schools may not pay a lot of money for the rights to produce a show, the sheer volume of the productions can return a significant amount of profit post Broadway.

In fact, sometimes a show many not recoup its investment on Broadway but will then recoup after years of touring or additional productions in the subsidiary markets. Shows with high subsidiary rights value can keep checks in Investors' mailboxes for years after the close of the original production on Broadway.

QUIZ!

1. What is the average number of shows that recoup on Broadway?
    a. 1 out of 100 or 1%
    b. 1 out of 10 or 10%
    c. 1 out of 5 or 20%
    d. 2 out of 5 or 40%
    e. No shows recoup.

2. How much should you be prepared to lose if you make a Broadway investment?
    a. 100%
    b. 20%
    c. 80%
    d. 0%
    e. Unlimited because you can lose more than your original investment.

3. Which of the following is NOT a way Investors can earn returns on their Broadway investment?
    a. High school productions
    b. National Tours
    c. Merchandise
    d. A movie
    e. The Director's speaking engagements

ANSWERS: 1(c), 2(a), 3(e)

Chapter Three

How Broadway Investing Works

In this next chapter, we're going to get into the nuts and bolts of investing in a Broadway show so that you have a clear understanding of what happens to your money after you write your investment check, as well as how and when that money is returned to you. Knowing the mechanics will help you sleep easier at night and eliminate some of the "anxiety risk" associated with investing in Broadway that I find so many first time investors have.

THE REQUIREMENTS FOR INVESTING IN A SHOW

Investing in a Broadway show is just like investing in any business. And when any founder of a company seeks to raise money for his or her business, there are rules and regulations governing the process of raising money, and who you can raise it from.

You're probably aware of the term Initial Public Offering (IPO), which refers to when members of the public are given an opportunity to purchase shares of a stock that is coming on the market. Generally speaking, under those types of offerings, anyone with a financial advisor or their own online investment account can purchase these types of securities. With just a few clicks of a mouse, you can be the owner of Facebook, Google or even a high-flying, high risk, penny stock.

This is NOT the case for Broadway shows.

Most Broadway show are "private" offerings and are not publicized or offered to the general public. Although the rules have changed a bit since the passing of The Jumpstart Our Business Startups Act (JOBS) in 2012 and some "general solicitation" and advertising is allowed under certain situations, most Broadway shows are not promoted, publicized or advertised to the general public.

Why can you buy a penny stock online and not invest in a Broadway show?

Companies that "go public" go through a much more rigorous regulatory process with the federal government and state governments both prior to the announcement and throughout the life of the company in order for their shares to be sold to the general public. This is an arduous and expensive process (translation: you need a lot of lawyers).

For my crowd-funded revival of *Godspell* in 2011, I raised money with a semi-public offering during which I was allowed to promote the offering publicly and raise money from more people than a typical private Broadway offering (although I was still restricted in a number of areas). While this process was worth it to me in the long run, it was a very difficult process that I'm not sure I would repeat. ((I also don't like to repeat myself with my marketing initiatives, anyway!)

Since "going public" is too expensive and too time consuming for Broadway shows, most Producers choose types of offerings that are less expensive to launch that have oversight and regulation but are therefore more restrictive in the types of Investors that can be approached.

Because these offerings are less regulated upon startup and because there is less oversight on an ongoing basis, the government established a set of rules governing WHO is eligible to invest.

The first step the government took when considering who should be allowed to invest in less regulated investment vehicles was to put investors into two differing classes or buckets. They are:

1. Accredited Investors

2. Non-Accredited Investors

According to the SEC website, the definition of an Accredited Investor is:

> Anyone who has earned income that exceeded $200,000 (or $300,000 together with a spouse) in each of the prior two years, and reasonably expects the same for the current year, OR has a net worth over $1 million, either alone or together with a spouse (excluding the value of the person's primary residence)."

A Non-Accredited Investors is anyone who falls outside of those parameters.

Next, depending on the type of offering a Producer applies for when raising money, the SEC dictates which class of Investor you are allowed to approach, Accredited Investors or both Accredited and Non-Accredited Investors.

The SEC assumes individuals of a higher net worth (Accredited Investors) are better able to understand the information necessary to make an informed investment decision than the less affluent (Non Accredited) Investors. Thus, when an offering includes Unaccredited Investors, more information is required to be provided, usually in the form of a Prospectus or Private Placement Memorandum.

How does this apply to investing in Broadway shows? <u>Generally speaking, most offerings to invest in Broadway shows are for Accredited Investors only.</u>

There are some exceptions to this rule. My production of *Godspell* allowed both Accredited and Non-Accredited Investors. Some offerings allow a limited number of Non-Accredited Investors.

As a potential Investor, one of the first things you must do is determine which bucket you fall into. Are you an Accredited Investor? Or are you Non-Accredited at the moment but on your way to Accredited status?

If you are not yet Accredited, there are other offerings out there, so don't put this book down. These types of offerings are just harder to find. When you are approached about investing in a show or when you approach a Producer, <u>one of the first questions you'll need to ask Producers is whether or not they accept Non-Accredited Investors.</u>

And remember, accredited status changes each and every year, so what I tell my Non-Accredited friends who want to invest is . . . let's figure out a way to make you some more money!

> NOTE: The definition of Accredited Investor I stated above is as of the writing of this book. This definition does change from time to time. In fact, prior to 2008, the value of your home could be used in the calculation of your net worth, which made it much easier to satisfy the accredited requirements. I know there are many discussions about modifying it again, so keep your eyes open. I've written about this often on my blog and will definitely do so again whenever there is an update, so sign up today at <u>www.TheProducersPerspective.com/subscribe</u> to make sure you are among the first to know.

If you'll allow me to get on a soap box for a few paragraphs . . . while I understand the SEC's desire and need to protect the Investor who doesn't have significant resources from fraudulent and misleading investment opportunities, I believe this law is too restrictive and too arbitrary for the Investor and the individual raising the money. Any person in this country, no matter if he has $10 or $100,000 to his name, can take a bus, hitchhike or drive to a casino (and there are casinos thirty minutes from just about everywhere these days) and bet his entire life savings and lose it all with NO accreditation status and no regulation. But that same person can't legally invest in a Broadway show, a hardware store, a restaurant, or any legit small business that uses private offerings? I've heard a few politicians say that small businesses are the backbone of this country. But I guess not. It's as if the government is saying that these potential explosive growth opportunities (many of which are less risky than a spinning a roulette wheel) are only for the really rich. And the small Investors can play all the Blackjack they want and buy all the Powerball and scratch tickets they can afford, even if they have no money for food after.

Let me be clear. We need regulation . . . but there should be a method of allowing Investors to qualify to make certain investments. Screening? A test?

Ok, I'm done. Off the soap box I come.

NOTE: Thanks to the passage of the JOBS Act in 2012, crowdfunding for Non-Accredited Investors became legal under certain regulations (because of my crowdfunded Godspell in 2011, I was interviewed by the Office of Congressional Oversight regarding the JOBS Act and how it would be implemented). While I don't expect the JOBS Act to be a source of funds for Broadway shows, it may become an option for Off Broadway shows with smaller budgets. For a white paper on the Jobs Act and crowdfunding, visit www.TheProducersPerspective.com/appendix

The Corporate Structure Of A Broadway Show

Many people think that because a Broadway show is such a unique "product," that it has its own set of business rule, regulations and structure. But the fact is, Broadway shows are just like any other small or medium sized business, and they are structured in the same way. So, if you own your own business or have invested in other businesses, you're probably more familiar with the structure than you think.

Broadway production companies invariably are formed either as Limited Liability Companies (LLCs) or sometimes as a Limited Partnership (LP). Both are pass through entities for tax purposes, meaning the gain and losses flow through directly to the owners rather being taxed at the entity level (as would be the case with a regular corporation).

LIMITED LIABILITY COMPANY

The Limited Liability Company is the most common legal structures used for Broadway productions. In an LLC, there are two types of members: Managing Members and Investing Members. In the context of Broadway investing, the Lead Producers are the Managing Members of the Company and Investors are Investing Members. As the name suggests, all LLC owners (Managing Members and Investing Members) are protected from personal liability for business debts and claims. If a business is organized as an LLC and the business can't pay a supplier, the landlord or any vendor service provider, that creditor cannot come after an LLC member's house, car, or other personal possessions and assets to recover the funds owed. Only assets owned or controlled by the LLC can be used to pay off business debts. Therefore, the owners of LLCs can only lose the money that they've invested—hence the *limited* liability. It would be pretty hard to get entrepreneurs to start any kind business in this country if they knew that every time, they took that risk and created jobs, employed vendors, paid taxes, etc. that they had the chance to lose their house, life savings, and more, which is why this type of entity was created.

Theatrical LLCs used to have more operating headaches (annual state fees based on the number of members, the publication of the LLCs formation, etc.), which were deterrents to some Producers. LLCs are less onerous today than they were, which is why they are the most popular entity used for Broadway investing.

LIMITED PARTNERSHIP

A Limited Partnership is the second most popular corporate structure used for Broadway productions. LPs were more popular many years ago simply because there was no LLC alternative. It was only in 1994 that New York authorized the LLC!

A Limited Partnership has two types of participants: **General Partners** and **Limited Partners**. In our context, the General Partner is the Lead Producer, and the Limited Partners are the Investors. The Limited Partners do not participate in the day-to-day management of the partnership (making decisions about advertising, ticket prices, etc.) and their liability is limited to only their initial investment, as we discussed previously (but do remember to look for the language that specifies this in your documents before you invest).

In contrast to an LLC, an LP only offers personal liability protection to certain partners. Full personal liability rests with General Partners (Lead Producers), meaning General Partners *can* be sued for debts incurred by the partnership. That's why it's rare for an individual to serve as a General Partner. Usually, the General Partner is a Corporation or LLC owned by the Lead Producer.

The Limited Partners (or Investors) in an LP receive the same liability protection as LLC members, which is the most important thing for an Investor to understand. Quite simply, as an Investor in an LLC or an LP, you cannot be liable for more than your personal investment.

OFFERING DOCUMENTS

Once the company structure is established, the "Offering Documents" will be drawn up by the Production's attorney. Offering Documents are exactly what they sound like. They are the documents that are given to Investors as an "offer to invest." These documents will include all of the details of the legal structure of the show, the "risk factors" (which inform the potential investor of the potential risks of investing), as well as how the Producer intends to operate the show financially. These documents can be very long and filled with legalese so settle into a comfy chair with a cup of coffee to make sure you stay awake while reading!

If you'd like to read a sample set of Offering Documents to give you an idea of what to expect when you receive your first set, visit www.TheProducersPerspective.com/appendix.

INVESTMENT SIZES OR UNITS

When drawing up the Offering Documents, the Producer will need to determine the price of a "Unit" in the production. In an LLC, Units might be considered similar to shares in a publicly-traded corporation. For example, if a production has a budget of $10,000,000, the show's Unit Price may be $100,000, in which case there would be 100 Units available ($10,000,000 divided by $100,000).

The unit price might also be $75,000, $50,000 or honestly, whatever the Producer decides! Most Investors don't realize that how a Producer determines the price of one Unit is completely arbitrary. That's right, Producers make it up! And how we decide that price is based on a Producer's individual style (and also some psychology but keep reading for more on that).

Some Producers I know simply divide their capitalization by a hundred, as in the example above, to get their Unit Price. Some like their Units to be set at $250,000 each, while others may fix each Unit at only $75,000. It's entirely up to the Producer. This Unit Price will be specified in the Offering Documents.

There are times a Producer sets a minimum investment level without dividing the Capitalization into units, but invariably will reserve the discretion to accept investments that are below the minimum level.

Now, I know what you're thinking. "Ken! You said it was possible to invest in shows for less than $100,000! Especially if I'm just starting out! I don't want to start off with a $250,000 or a $100,000 investment!"

Don't worry. You don't have to.

High priced units are one of the biggest reasons why so many people believe that Broadway investing is only for the super-rich.

What you must understand about Units, and this is something that is <u>not</u> advertised, is that Producers have the option to break those units in halves, quarters, eighths or whatever he or she would like.
So, you may have the open to purchase one half or even one quarter of a $50,000 unit. Or maybe even less! Just don't depend on a Producer to offer this to you. You may have to ask.
When you receive a set of Offering Documents from a Producer and you notice that a Unit Price or a minimum investment level is higher than you are comfortable with, don't drop the documents, run away and say, "No way am I ever investing in Broadway if that's the amount of capital I have to risk." Instead, ask the Producer if you can purchase a fractional share of a unit (one half or one quarter, etc.). Don't be embarrassed, or think that you are out of your league. Fractional investing is very common.

Now, do remember that fractional shares of units are up to the discretion of the Producer. He or she may say no to your request, but it is always worth asking the question if you are uncomfortable with the Unit Price, or if you are interesting in holding back some capital for other investments.

TIP: Need to convince a Producer to take a fractional investment? Try this. Just say, "One of the reasons I'd like to get one half of a unit is I'd like to be able to consider investing in your next project if you have something to invest in before this one recoups." Producers are always worried about raising money for their next show.

Purchasing a full Unit when an investor doesn't want to is one of the most common mistakes that first time Investors make, and it can cost them thousands of dollars and scare them off investing for good. If you want to make sure you only invest what you're comfortable with, the key to remember when asking about a possible investment is **not** to ask the Producer, "What is the price of each Unit," when you are inquiring about an investment. Instead, ask "What is the **minimum investment** you will accept?" There is a difference!

This slight change in how you ask the question could save you a great deal on each investment you make, giving you more capital to diversify your investments and therefore more chance to find a hit.

Of course, if you take a half a Unit of a show that becomes the next *Wicked*, you're going to regret not taking that full Unit for sure. So don't blame me!
The key to determining your amount is to ask about all your options when investing. This is not a time to be shy. This is high risk investing! Producers should want to explain the process and only accept an investment that an Investor is comfortable making. A Broadway Producer should be interested in a long term relationship with you, not just getting you to write the biggest check possible. So find out your options. The more options you have, the smarter a decision you can make, and the more you mitigate your risk.

IF YOU CAN GET IN CHEAP, WHY ARE THE UNIT PRICES SO HIGH?

Here's where psychology comes in. The more an Investor invests, the less the Producer has to raise from other Investors. Many people will invest the full Unit price (or purchase multiple Units) with no questions ask, which makes the Producer's job easier. A higher Unit Price also gives a Producer more room to negotiate with those Investors who want fractional Units. It's the psychology of pricing.

While this may be a good sales technique if you're selling real estate or hot tubs, I don't believe in this strategy for high risk enterprises like Broadway investing, which is why I try to always keep my Unit prices around $25,000 and sometimes even lower.

HOW AN INVESTMENT AFFECTS YOUR TAXES

At the end of each year of operation, the LLC is required to provide each member with a Schedule K-1, which breaks down each member's share of the LLC's profits and losses. In turn, each LLC member, or Investor, reports this profit and loss information on his or her individual Form 1040, with Schedule E attached.

Unlike a corporation, an LLC is not considered separate from its owners for tax purposes. Instead, an LLC, like an LP or sole proprietorship, is what the IRS calls a *pass-through entity*. This means that business income passes through the business to the LLC members, who in turn report their share of profits—or losses—on their individual income tax returns.

You should always talk to your accountant about how an investment—whether it's successful or not—will impact your taxes. But as a rule of thumb, expect to pay taxes if the show is profitable and expect that you will be able to write off a loss if not (exactly when you can take the full loss is subject to the accounting of each production). As we discussed in the reasons why people invest in Broadway shows, if your show does not achieve profitability, it could result in tax savings for you just like a loss in a stock or another traditional business. You'll still have a loss, but the tax savings can make it less painful.

Please remember, everyone's tax situation is different. Therefore, we strongly advise you discuss your interest in investing in Broadway productions with your Accountant before you invest. Just be prepared for them to tell you it's too risky. Then give them this book.

HOW AND WHEN YOU MAKE MONEY INVESTING

One of the primary reasons that people don't believe there is a possibility for Investors to make money on Broadway is that they simply don't understand what happens to the money after an audience member pays for a ticket and how that money flows back to the Investors. While Broadway accounting and its business structures are nowhere near as complicated as Hollywood accounting, it can be difficult to comprehend if an Investor has not invested in a similar industry before.

In this section we're going to discuss exactly how a Broadway Investor like yourself can earn money (and exactly how much) on their investment.

First, it's important to understand that there are two types of budgets on Broadway, a **Production Budget** and an **Operating Budget**.

The Production Budget, often referred to as a show's capitalization, is the number that you've probably heard most often quoted in the press, or bandied about by Producers or other Investors. For example, you may hear, "*Phantom of the Opera* cost $8 million", "*Wicked*'s capitalization was $14 million," or "*Spiderman* cost $83 million."

The Production Budget is the total amount of money needed by a show's Producer to get the show from the very first seed of an idea all the way to opening night. Or, to put it in small business terms, a Production Budget is what it could cost an entrepreneur to open the doors and start accepting customers at a restaurant, a doctor's office, or any business.

In the Production Budget, you'll find development costs (workshops, readings, etc.), audition expenses, rehearsal costs, the costs of building the scenery, etc. and even the opening night party. Every dime that is spent getting the show to opening night is included in the Production Budget.

The Production Budget is also the amount of money that will be raised by the Producer from Investors, and is the amount that will need to be recouped. To give you some perspective, as of the writing of this book, the average Production Budget for a new musical in the current Broadway era is around $13 million to $15 million and new plays can cost anywhere from $3 million to $4 million. These numbers are a generalization, and budgets can vary widely depending on the show. If you come across a show that is outside these general numbers, the important question to ask the Producer is, "Why does this production cost more (or less)?" There are a number of factors that could shift these figures in either direction. The important factor for you to consider is why. A budget that colors outside the lines does not mean the show should not be considered for an investment.

The Operating Budget details the amount of money that it will take to run the show on a weekly basis, once the show is in performances. It consists of the salaries of all employees, advertising expenses, theater rent, equipment rentals, etc.

The Operating Budget, also referred to as a show's "nut," is arguably the most important part of a production's financial operations. The Operating Budget is the amount of money you'll need to earn through ticket sales per week in order to be profitable and stay in operation. If a show doesn't make its "nut" for several weeks in a row, it might be necessary to close the show prematurely. Ironically, the Operating Budget is *not* the number talked about in the press as much as the Production Budget. Why? People (especially the press) like to talk about BIG numbers, even though the smaller weekly Operating Budget has much more of an impact on the financial viability of a show. (In the upcoming chapter, "Strategies for Success," we're going to discuss how analyzing a show's Operating Budget is one of the most important parts of your due diligence process when considering an investment, and I'll give you a simple tip to help determine the viability of your potential investment.)

For example, if a show's operating expenses are $600,000 and you sell $1,000,000 worth of tickets, then you have a healthy $400,000 worth of profit. But if you only sell $200,000 worth of tickets, then you've lost $400,000. Shows can't operate for too long on those kinds of losses.
A Broadway show's Operating Budget can vary widely depending on the size of the cast, whether or not there are stars in that cast, the number of costume changes (more changes equals more Wardrobe staff members), orchestra size, etc. For example, you can bet that *Dear Evan Hansen* with its cast of eight on stage and simple set costs a heck of a lot less to run each week than *Wicked*! Generally speaking, the average running cost for a Broadway musical is probably around $600,000 to $700,000 thousand per week. Plays average around $300,000 a week to run. Just like Production budgets, these figures can also vary significantly, although I find there to be less of a variance because they are somewhat based on the fixed number of seats in a theater and the fixed number of performances we're allowed to do each week (eight).

Again, if a production you're considering has an Operating Budget that is outside these parameters, ask the Lead Producer if there is a specific reason as to why, which will help you determine the risk level of the production. Remember, the Operating Budget is the most important factor in the long term financial viability of a Broadway show (or restaurant, hardware store, etc.). If you can't keep a show running, it doesn't matter how cheap (or expensive) it was to open.

IT'S JUST LIKE YOUR OWN LIFE!

Confused? Think about a show's Operating Budget like the cost of living your own life. What does it cost to keep your own life running? You have rent, groceries, gas, entertainment, etc. Those total costs are like your own personal Operating Budget. And you need to earn enough through your job, investments, etc. to cover those expenses. Any amount you earn over that "nut" goes to your savings.

The same is true on Broadway. Except that the money that would go to into your savings account is the money that goes back to the Investors.

How You Get Your Money Back

If a show is profitable on a weekly basis, and there is enough money in the show's reserve account (which is an amount the Producer keeps in savings in case there are any financial surprises like weekly losses, additional advertising opportunities, etc.), the show will begin to distribute that money back to its Investors.

One of the benefits to Investors in Broadway shows is that prior to recoupment, 100% of weekly operating profits after all expenses are paid go back to the Investors.

So, in the above example, if the Production earned $400,000 in profit over five weeks after all expenses were paid, the show would have a total of $2 million in profit. That money could be distributed to the Investors by the Produce, again, provided there was a healthy enough reserve fund and the Producer and General Manager were forecasting more profitability in the future.

Since we know 100% of profits go back to investors, you would receive a pro-rata amount of that $2 million based on the percentage of the Production Budget or Capitalization you invested.

For example, if you invested $1 million of a $10 million production, you invested 10% of the capital, which means you'd be entitled to receive 10% of that $2 million profit or $200,000.

Provided the show continued to be profitable, this process would continue until the show recouped its entire $10 million Production Budget (which means you would have received your entire $1 million investment back.)

SO YOU REACH RECOUPMENT – THEN WHAT?

The holy grail of producing is recoupment, which is the point at which the producer has earned back all of the expenses of producing the show.

> NOTE: When a show recoups, you still may not have *received* your entire investment back. Remember, because a show keeps a reserve or a "rainy day fund," it may actually cross the line of recoupment into profitability before the full amount of an investment is returned. Producers often like to announce recoupment as soon as it occurs on paper to generate press and trumpet the financial success of the production. If a show announces recoupment, you can rest assured that you will get whatever is left outstanding on your investment back in due course. A Producer wouldn't announce recoupment without knowing your money was coming back to you very soon.

As we discussed in the previous section, prior to recoupment, 100% of the profits are returned to the shows Investors. But what happens after recoupment?

Traditionally on Broadway, all profits after recoupment are split 50/50 between the Managing Members (or Lead Producers) and the Investment Members (or Investors). Post Recoupment is when Producers receive the majority of their compensation for producing a show. While there are some fees and royalties paid to Producers during a show's run both before and after recoupment, none of those fees and royalties compare to the profits a Producer can receive after recoupment. This payout structure incentivizes Producers to get to recoupment as fast as possible, so they can earn their profit.

CALCULATING A SAMPLE RETURN

Let's use a hypothetical example to demonstrate how to calculate a Broadway return after recoupment. Imagine you invested in a new Broadway musical. The capitalization of that musical is $10 million and you invested $1 million, or 10% of the capitalization. The show opens, recoups, and post recoupment, plans to distribute $1 million in profit to its Investors.

Got your pencils out? It's like a Broadway investing SAT question!

How much of that $1 million profit distribution do YOU receive for your $1 million investment?

Because the show has recouped, that $1 million of profit gets split 50/50 with $500,000 distributed to the Managing Members (Producers) and $500,000 distributed to the Investing Members. If your investment was $1 million, or 10 percent of the capitalization, your share of the Investors' profits will be $50,000. In simple formula terms, after recoupment your return will be:

(Profit x .5) x (your percentage of capitalization)

The common mistake in this calculation is to think that your return is the percentage of your investment multiplied by the *gross profit* distributed. Don't forget that *after recoupment*, the gross profit is split in half with the Producers first and then you receive your pro-rata percentage share of the other 50%.

WHEN ARE DISTRIBUTIONS MADE?

The schedule of distributions is another very common questions I get from Investors who are considering in investing in one of my productions. Investors often believe they have to wait until a show recoups its full capitalization before any money is distributed to Investors, This is a common misconception.

Distributions (the return of capital (prior to recoupment) or profit (post recoupment)) are made at the discretion of the Managing Member, subject to certain guidelines set out in the Operating Agreement of the production. The Managing Member will distribute money back as soon as the Member feels there is adequate money in reserve to run the production and have a buffer for a rainy day.

To protect Investor profit, it is important that Producers distribute money to their Investors when a show has a comfortable reserve and no more. A proper distribution schedule ensures that future losses can't eat away at previously earned profit.

TIP: Before investing, ask the Producer how much of a reserve he plans on keeping before making distributions. While there may not be an exact answer to this question at the time you ask it, it will give you a general idea as to the Producer's style and methodology for making distributions.

Successful shows with great reviews, Tony nominations or awards, etc. can earn significant profits very quickly after opening, in which case you might receive a distribution fairly early in the show's run. (One of my favorite things to do is to make a distribution on opening night of a production!) However, if sales cool down after opening, you may have to wait a few months before the next distribution, while the show builds its reserve.

If a show reaches a point of more constant and reliable profitability, you may receive distributions on a more regular schedule, such as quarterly or even monthly.

Do not expect any reliability or predictability of distributions early on in a show's life. It is not until a show's trajectory and financial footing have been established before a schedule can be determined. Even then, the amount of the distributions may vary widely.

QUIZ!

1. Prior to recoupment, what percentage of profit do the Investors receive?
    a. 25%
    b. 50%
    c. 100%
    d. 75%
    e. 0%.

2. What is the price of a Unit on a Broadway show?
    a. $25,000
    b. The Producer decides.
    c. The Attorney General of NY decides.
    d. $100,000
    e. The Capitalization divided by the number of Investors.

3. When are distributions made?
    a. Only after a show recoups 110% of its investment
    b. Only after a show recoups 90% of its investment
    c. When the SEC mandates
    d. At the discretion of the Lead Producer, depending on what is in a show's reserve fund.
    e. At the discretion of the General Manager, depending on what is in a show's reserve fund.

ANSWERS: 1(c), 2(b), 3(d)

Chapter Four

Strategies to Increase Your Odds for Success

Now we're getting to the good stuff. One of the core principles of my business (and my life!) is the belief that no matter the endeavor, there is *always* a way to improve your results. If you make the effort and are committed to education, then it doesn't matter if you are learning how to speak Spanish, play golf or invest in Broadway shows, you can and will become a better Spanish speaker, golfer, and yes, Investor.

In this chapter, I'm going to teach you strategies that you can use immediately to improve your results when you invest in Broadway shows. The methodology I have developed is based on my experience over the last twenty five years of my career on Broadway as a General Manager, Producer and as an Investor. It is the same system I've used to beat the industry average and recoup more than 40% of the shows I've produced or invested. (And a few of the shows I have been involved in that did not recoup were shows that my Investors and I did not *expect* to recoup. We chose to invest in the show to support the art and the artists involved regardless, because of how important we felt it was to get that piece of theater out in the world.)

Why do I believe these strategies can help you or anyone looking to make smarter investments in Broadway shows?

Simple.

As we stated earlier, the average rate of recoupment is one out of five or 20%. *That's the average*. In other words, my puppy could pick one out of five shows and find the one that recoups. So doesn't it make sense that if we study the history of investments, examine a show's financials, identify trends in hits, and so on, that we should be able to do better than the average? Of course it does!

Since there are so many factors on Broadway (and in any business) that are beyond our control, we will never be able to eliminate risk from Broadway investing (or any kind of investing). But there are many ways to reduce that risk . . . or at least *understand* the risk before we invest.

If you wanted to invest in the stock market or in a start-up or in a hedge fund, you wouldn't just pick a name out of the newspaper and write a check. At least I hope you wouldn't. Instead, you would conduct due diligence and find out everything you could about the particular company. You'd look at the entire industry. You'd check for recent trends. You would research the owners of that new start-up and see what kind of track record they had for opening new companies. You would investigate the past returns of the hedge fund and look to see if any complaints had been filed with the Securities and Exchange Commission. <u>You would take your time to make sure you were making the best decision for you, your financial situation and your personal goals.</u>

And most likely, if you don't have the time, or can't do the research above, you would find an Investment Advisor (which in the theatrical world is a Producer) to do the due diligence for you in order to give you the information you need to make the decision that is **best for you**.

And that, my Broadway investing friends, is the most important thing for you to understand. Despite the method I'm going to describe for you now, this system will never result in an absolute "Yes" or "No" or "Invest" or "Don't Invest" at the end of the process.
Many hedge funds and e-trading companies on Wall Street have algorithms that tell traders when to buy or sell, and they are wrong all the time. Since every investment decision is different for every Investor, I would never recommend any kind of blanket policy of when to invest in a show or not.

I know far too many people who have said to me, "I just invested in *Insert Show Title Here* and it's gonna make so much money." A few months later, the show has closed and the investment is gone. I also know plenty of people who have been told, "Don't invest in that, you'll lose every penny." Nine months later, the show recoups.

That's why no Producer can ever guarantee a hit. There are far too many variables including competition, critics, current events, and most importantly how the audience responds to the show once the curtain goes up on opening night and how quickly and passionately they tell their friends to see the show (because word of mouth is and always will be the #1 driver of ticket sales in the theater). And that's something we can never predict until we actually raise the curtain!

Also, remember, Broadway shows are "non-essential" purchases. We don't need to see a Broadway show to survive. We all need a house, which is why real estate has always been such a stable investment. The sweet spot of investing is when a "non-essential" purchase, like a show or a book or a handbag becomes a "must." That's the type of market penetration all Producers and Entrepreneurs are looking for.

While I can't guarantee how the market will respond to a show, I can guarantee that we can determine the level of risk of a production and then decide whether or not we're interested in taking on that risk. And by doing so, we should be able to choose winners more often than the one out of five show historical average on Broadway.
This is the same philosophy Financial Advisors use when choosing investments for their clients. They want to "beat the market." As do I. My goal is to recoup *more* than 20% of my shows (so far, so good) and to maximize profit, just as a Financial Advisor's goal is to beat the S&P's return. My goal is not to win awards or get great reviews, unless I believe those things are part of the strategy to help the show recoup. I

know I'll never be right 100% of the time. But I should be able to do better than the average.

TIP: Determine what is most important to the Producer you're considering investing with before you invest. Are they profit driven? Awards driven? Make sure your Producer's goals are married with your own.

Here is the system that I use to beat the Broadway market, and how you can use it to improve your results.

WHAT MY SYSTEM HAS IN COMMON WITH MY ELEMENTARY SCHOOL NEWSPAPER

The system I use as the foundation of my due diligence process is based on the principles I learned from writing articles for my school newspaper. My teacher taught me to ask myself the famous five W's when researching any story: "Who, What, Where, When, Why" . . . as well as the 1 H, "How?"

I've adopted that same system to help determine whether or not I should invest in a Broadway show. (By the way, this system isn't just for Broadway investing. It can be applied to any type of investing or business proposition. I urge you to give it a shot. You'll be amazed at how it distills a lot of information down to a more digestible set of facts that allow you to make a more informed decision.)

Every time a new Broadway opportunity comes across my desk, I go through a checklist based on those W's and 1H, and ask myself:

- Who?
- What?
- Where?
- When?

- Why?

And . . .

- How MUCH???

Let me break down each of the "W's" (and that one important "H") so you can understand how they relate to Broadway shows.

WHO?

As you might guess, when I'm raising money for shows, "Who is in it," is the first question I'm usually asked by a potential Investor who is interested in learning more.

And while of course the names of the actors in a show is an important part of the *Who*, it's 101% NOT the first question potential Investors *should* ask. Here's why:

Sure, name brand actors or Stars can be great "insurance policies" for shows, because they can sell tickets just by announcing their involvement with a show, as well as generate publicity for the show through articles, interviews, etc., which doesn't cost the production money (except for that high Star salary, of course). However, historically, stars do not drive the largest investment returns on Broadway. This is due to a number of factors, including their large salaries (which often includes a percentage of ticket sales), the limited amount of time they are willing to commit to the production, the difficulty in replacing them after their contract is up, etc.

When you are looking at an investment opportunity, you have to decide whether you want the insurance policy of a Star name in your cast, which reduces your risk at the launch of your show, or if you are looking for a large, long term return on your investment and are willing to take the risk that comes with that kind of investment. Because stars do NOT historically deliver the largest returns.

Need some proof? Let's take a look at this list of the longest-running shows of all time as of this printing:

1. *The Phantom of the Opera*
2. *Chicago*
3. *The Lion King*
4. *Cats*
5. *Les Misérables*
6. *Wicked*
7. *A Chorus Line*
8. *Oh Calcutta!*
9. *Mamma Mia!*
10. *Beauty and the Beast*

Notice anything?

Not one of them . . . not one . . . opened with big stars. (*Chicago*, which is the only revival on the list, did have a few Broadway stars in its cast, but no Hollywood stars.)
The longest running shows of all time are also some of the most profitable shows of all time. That's why I believe that if you are looking to invest in a big, *Les Miz*-sized hit (and who doesn't), then you actually do NOT want a Star in a show you're investing in.

Instead, you want the SHOW to be the star.

If the show is the star and becomes a hit, then audiences could but tickets for decades (e.g. *Phantom of the Opera*) regardless if the original cast is still in the show, or whether or not an understudy is performing. A show without stars also increases the ability and ease of franchising the show in theaters throughout the world (remember subsidiary rights income?).

What is also interesting about the shows on this list of longest-running shows of all times is that many of them MADE stars of people like Donna McKenchie, Idina Menzel, Michael Crawford, Betty Buckley, etc.

To achieve the highest returns, don't cast stars. Make them instead!

So if the cast is not the primary concern of the *Who* in my due diligence process, then who is?

One of the first *Who's* I examine when determining a show's risk level is, "Who are the Authors? Are they rookies? If they have written for Broadway before, *what is their recoupment record?"* Obviously a show by Andrew Lloyd Webber has less risk attached because of his recoupment track record, than a show by an unknown composer.

This said, please note, many first time Composers and Lyricists *have* had tremendous success on Broadway. The very successful Producers Kevin McCollum and Jeffrey Seller, who produced the Tony Award Winning Musicals *Rent, Avenue Q,* and *In the Heights,* achieved enormous success by giving the writers of those shows their Broadway debuts, despite the higher risks of going with unknowns.

In addition to doing research on the Authors, I also find out *Who* is directing? What is the Director's recoupment record on Broadway? Does the Director have a record of getting good New York Times reviews? (I find that there is a tendency for critics to support artists throughout their career, especially if they've helped discover them.)

And during the "Who" phase of this process, I of course as myself, "Who is the Lead Producer?" What is their track record? What are their goals? Do they have a reputation for treating Investors well?

When you start off investing, you may find yourself talking to a Co-Producer or a Broadway Bundler (more on these soon) rather than the Lead Producer. If you are not talking to the Lead Producer, make sure you do research on who the Lead Producer is. But also find out if you can get him or her on the phone? Are they accessible? Do they answer emails? Do you like them? Do you trust them? Remember, a Lead Producer is your Broadway show's CEO, and just like a Financial Advisor would study who is on the management team of a company or a mutual fund before investing, so should you.

You can and should continue to ask the "Who" question for the entire team of your show, from the General Manager to the Advertising Agency to the Production Manager, etc. One of my first Investors taught me you should invest in people, not in projects. This sentiment has been echoed by just about every major Investor I've spoken to in every industry, from private equity to real estate.

WHAT

Is the show you're considering investing in a play? A musical? A revival of a play? A revival of a musical?

These different types of productions have very different life cycles on Broadway and *after* Broadway which should play heavily into your decision as to whether or not you invest.

NEW OR REVIVAL?

Before we even discuss a play versus a musical, let's draw a distinction between a new production and a revival. Without looking at any other factors (cast, underlying source material, etc.), generally speaking, most revivals are lower risk than new productions because they have been produced before. There is usually some knowledge of the title amongst theatergoers. Also, the material (script, score, etc.) has been tested. You can read reviews of previous productions, evaluate how the show has done in the subsidiary market, examine its awards history, etc. A revival opens on Broadway with a pre-established brand and theatrical reputation (*The Iceman Cometh, Guys and Dolls,* etc.).

But nothing is free in this business or in any business, and you will "pay" for the decreased risk of investing in a show that has that brand by giving up what could be the most valuable part of any Broadway investment . . . subsidiary rights income.

As we discussed, when you invest in a new production, you are investing in the first of a potential franchise, and in addition to touring opportunities, you will customarily have a right to "subsidiary rights income" from regional theaters, community theaters, etc. for many years after the initial Broadway production has closed. This can be quite lucrative for Investors.

When you produce a *revival* on Broadway, more often than not, you are not entitled to *any* post Broadway revenue from licensed productions. Why not? Remember, you are licensing the right to produce the show on Broadway from the authors. Those authors may be paying other Producers a share of their subsidiary rights. Therefore, their response to a request for subsidiary rights participation from a Producer of the revival is usually something like, "Sorry, but this brand has already been established. We don't need this Broadway production to get the show produced at theaters across the country or around the world. It's already happening."

This is the trade-off for producing a revival with a pre-existing brand. Your upside is therefore limited and must be taken into account when calculating the risk of a production.

The above notwithstanding, recently some Producers have pushed back on this argument from the Authors by saying, "I understand your brand has been established. But, because of the marketing, advertising and press attention that this production will receive, your subsidiary income could increase. Therefore, shouldn't our Investors be entitled to *some* of that income?" (This argument is stronger if it's a show that has never been revived and the Authors are looking for helping in boosting the number of productions around the world,)

In some cases, Authors have accepted this argument, and given the Investors of a revival "Excess Subsidiary Rights Income." This is a formula that gives the new production a portion of subsidiary income *above* the average income over a predetermined period of time. For example, if the Authors received an average of $100,000 in subsidiary income over the previous five years prior to the revival, and after the revival they received $200,000, the revival Investors would receive a percentage of the excess amount, or $100,000 ($200,000 less $100,000). Typically this percentage is around 25%, instead of the usual 40% Investors would receive on all income for new productions.)

> TIP: If you're investing in a revival, ask if you will have any participation in subsidiary rights, including if the show is made into a film, TV show, etc.

PLAY OR MUSICAL?

You may have noticed that there were no plays on the longest running Broadway show list above. Open-ended run musicals (musicals with no predetermined closing date that run as long the show keeps selling tickets) are the biggest long-term money-makers on Broadway, which means they have the most upside for Investors.

These days, plays, especially revivals of plays, are usually produced for a finite period of time. (e.g. 12, 16 or 20 weeks). This limits the amount of money you can make, because of the number of seats in the theater and the fixed number of weeks the show is set to run. Therefore, a play's upside is also more limited, and in some cases, has an absolute “cap,” or ceiling.

That said, the limited run may actually make the production *less* risky because there is an inherent scarcity of tickets, which could increase demand for tickets during the window of a show’s run.

That’s why I often refer to investing in plays “smash and grabs,” as typically an Investor is looking to make a small profit in a short amount of time. That small return over a short run, when annualized, can translate to a very healthy return. For example, I was a producer on Will Ferrell’s *You’re Welcome America* and in an eight week run the Investors received a return of approximately 40% in profit after recoupment. Not bad, right? Even a 10-20% return over 20-26 weeks would be a very healthy return, considering the average growth over the last ninety years of the S&P 500 for a full year has been 9.8%.

AND DUH, THE “WHAT?” ALSO REFERS TO. . .

Of course the “What” question also requires you to dig in to the actual script and/or score of the show! Make sure you love it, but more importantly when considering a potential financial return, ask yourself, “Would I pay full price to see this show, and would I recommend my friends do the same?”

WHEN

I divide the Broadway Calendar into three “trimesters’ when examining the “When” of Broadway investing and producing. Each trimester has their own distinctive features that Investors should consider before writing a check.

1. Fall

While technically the Broadway season officially starts as soon as the Tony Awards are over in the middle of June, the "back to school" season of fall is what most people think of as the start of the new season. This is when you'll see "Season Preview" issues in the newspapers, magazines and websites that cover the theater.

One of the benefits of opening a show in the fall is that the show is one of the first out of the gate for the early adopter ticket buyers (and very important "buzz" starters). In addition, fall shows are the first of the season for our critics as well as our audience members, which means fewer shows to compare it to. Fall shows have more of an opportunity to "set the bar" for the season.
Shows that open in the fall also get the benefit of two of the highest grossing weeks of the year for Broadway as a whole: Thanksgiving and Christmas/New Year's.

One of the downsides to a fall opening is that the Tony Awards, which are held in June are many months away. Shows that are fortunate enough to get nominated can receive a tremendous amount of national publicity (and national attention is always challenging for Broadway shows to get). However, to for a show to run long enough to make it to the Tony Awards telecast with the hope that it will be nominated, a show opening in the fall will have to get through January and February, the doldrums of winter and some of the slowest months of the Broadway year.

So, if a show you invested in opens in the fall and show and doesn't open to strong ticket sales, it could be challenging to make it to awards season. Ironically, a show like this needs the attention that comes with the Tony Awards to boost sales, provided it can get there! See the business dilemma?

If you think the success of the show you're investing in is dependent on awards or the attention that goes along with that kind of publicity (including a number on the Tony Awards telecast, press articles about nominations, etc.), then a fall opening may be more risky than a spring opening. Additionally, the fall is the 2^{nd} most popular time to open shows, which means there is more competition for audiences.

1. Spring

The spring is the most popular time of year to produce shows, mostly due to the short length of time between a spring opening and the Tony Awards. If a show doesn't get good reviews or doesn't have strong word of mouth, then a Producer only has to wait a short period of time before awards season. The Tony Awards are one of the final weapons (and one of the most powerful) in a Producer's marketing arsenal that could turn a production around. If the show receives few or no nominations or awards after a spring opening, the show can close quickly before too much financial damage is done, as opposed to shows that open in the fall.

A few years ago, I analyzed the number of awards and nominations shows received based on opening in the spring versus opening in the fall. The results did prove that a show is *more* likely to receive a nomination (and therefore awards) if that show opened in the spring. (You can read that blog entitled, "Do Tony Voters Forget the Fall," by visiting our online appendix at www.TheProducersPerspective.com/appendix.)

This data is exactly why many will argue that producing and investing in a spring show is the least risky of all.

But that's only half of the story. Opening in the spring ain't all roses and less risk.

Because of the popularity of opening in the spring, competition is *extremely* high during this period. And while March and April can be strong months for ticket sales on Broadway (thanks to Spring Breaks, Easter, etc.), May and early June can be very challenging, as tourist season has not yet begun, families have graduations, dance recitals, christenings, etc. Because of the popularity of opening in the spring, the spring can have more shows for people to see, but less people actually looking to see shows! Unless a show has tremendous momentum, the late spring can be a very difficult to withstand.

Additionally, because of the number of new shows trying to open before the Tony Awards nomination deadline (usually at the end of April), there can be a new Broadway show opening every single night leading up to that deadline. During these few weeks, our critics are working overtime. Imagine seeing a new show night after night after night. It might sound glamourous, but after a while, it can be extremely tiring, especially for a critic who has to analyze and write about every single one.

There is also a greater chance that you'll be compared to the many other shows that the critic just saw. And if a critic just saw *Hamilton* on Monday and sees a show you've invested in on Tuesday, well, you could be in for a tough comparison.

In a crowded time of year, it's also difficult to get attention from the press because they have so many shows to cover. It can be harder to for a show to get a story on the front pages, as opposed to other times of year. And stories about shows sell more tickets than advertisements for shows. During less crowded times of year, a show may get front page coverage for a story that might have been buried on page fifteen at other times of the year.

2. Summer

The summer is one of the least crowded times of the year to produce a show on Broadway.

In the past, shows rarely opened in the summer. However, June, July and August are becoming more popular as of late, especially since

Producers are having trouble booking theaters during the more traditional times to open a show.

Conventional wisdom suggests that a show shouldn't open in the summer because the local audiences that are so important for starting a buzz in the NYC market are often on vacation and not in the city. And sure, tourists are in town over the summer, but they usually flock to titles they know more about, instead of the newest Broadway show that may not be on their radar as of yet.

However, there are some advantages to opening in the summer. First, there are fewer shows opening in the warmer months, so competition for audiences looking for something new is very low, and the critics are looking at shows with a fresher eye.

Also, as simplistic as this sounds, people tend to be in a better mood during the summer, so I find word of mouth and critical response to be buoyed by the positivity of the warmer vacation season. And what many people don't realize is that the summer has produced some extraordinary hits including *Avenue Q, Hairspray* and *Hamilton*.

That said, a summer opening is not for the financial faint of heart. Shows considering summer openings should have a strong brand, or should have just had a well-received Off Broadway or "in-town" tryout that has generated a lot of buzz. And summer shows should have a large reserve fund in their budget.

WHY

In order to resonate with the public, generate word of mouth and sell tickets, a show needs to answer the question as to *Why* it is being produced, and more specifically, "Why now?"

This is especially true for a revival. New shows can be produced simply because they are new. But a revival has to have much more of a reason for being produced again because of the amount of competition on Broadway. If you have one theater in your hometown, it may be fine to do *Annie* or *Guys and Dolls* for the twelfth time, but that won't work on Broadway. Audiences have so many other options of shows to see, including new ones. Being relevant and having a great answer to the "Why Now?" question can often mean the difference between a successful show, and one that an audience avoids.

Remember, when you are deciding whether or not to invest in a show, you are not investing in a vacuum. It's not good enough to know that your show is something audiences will want to see. <u>They need to want to see your show over other options that are available to them</u>. This includes new shows, old shows, and any other forms of entertainment available to them, including museums, standup comedy, live music, etc.

That's why the Broadway productions you invest in need to be different from the others and somehow resonate more (especially with the critics) in order to be successful.

A great example of this is the longest running revival, *Chicago*, which came back to Broadway at a time when the world was obsessed with super-slick lawyers getting their clients off for dastardly deeds. (The world had just watched the infamous OJ trial on television before the revival opened.) The show was a timely comment on what was happening in our society, all wrapped up with some "Razzle Dazzle" which helped the production become one of the longest running musicals of all time, and consequently, delivering substantial returns to the Investors to this day! The original production of *Chicago* ran for only two years. The revival has been running for over twenty years. The revival answered the question, "Why now," and the genius Producers, Barry and Fran Weissler, have done a brilliant job of keeping the show relevant over the years (partly through their creative star casting), and created a global phenomenon in the process.

The *Why* of a show can be one of the most important questions to answer in the due diligence process. If there isn't a compelling reason why the show *must* be produced now, the investment becomes much riskier.

WHERE

Broadway is a very concentrated geographic destination. All of the Broadway theaters (except for Lincoln Center) are located within a 13 x 2 block area in the center of Times Square. Since so many of our theaters are in such a small area, you wouldn't think that location matters much, but it does.

The old real estate adage "Location, location, location" matters for theaters too. For example, I call 45th Street between Broadway and 8th Avenue the "5th Avenue" for theater shoppers, since it is the most dense block of Broadway theaters. There are six theaters on that block alone! If you have a show on that block, thousands of theatergoers are going to walk past YOUR marquis on their way to see whatever show they have tickets for. That's a lot of free advertising and it can have an immediate effect on sales and word of mouth. How many times have you walked by a theater, looked at the marquis or the photos outside a theater and said, "I want to see that!" In fact, I once was Company Managing a show on this block and a tourist came in to the box office and said, "Please give me one ticket. I have to see a Broadway show before I leave tomorrow." He didn't even know what was playing at this theater! He just walked in, put his credit card down, and purchased a ticket. Just because he was walking by this theater on this block!

NOTE: When a Producer rents a Broadway theater, he or she can put up signs, posters, quotes, and of course a marquis for no additional costs. It's including in the rent. Since outdoor advertising in Times Square is very valuable, this 'signage' can be very valuable. This is why when a show closes, the next show moving into the theater will rush to have their materials installed immediately. Every day without it installed is wasted advertising potential.

Now, is a location going to make the difference between a show becoming a smash hit or flopping? No. *Rent* famously opened at the Nederlander Theater on 41st Street where no one thought anyone would go to see a show. But *Rent* proved that when a show is good enough, customers will go anywhere.

While the location ultimately won't make a recoup-or-not recoup difference, it does decrease the risk if you are in one of the theaters that gets more walk-up traffic than the others. And a more trafficked location could result in a few more percentage points of a return if your show doesn't recoup. (Making 60% of an investment back versus 50% would be a better result, right? On a $50,000 investment, this would mean another $5,000 in your pocket!) If a show you're considering in is opening in one of the theaters on 44th Street between 6th and 7th Avenues (like the Belasco or the Hudson), that show may not get as much foot traffic as other theaters. As always, this one factor doesn't mean you should not invest. This production just might not have the slight location advantage that another show might have. And perhaps you should look to see if there are other elements of the show that will help balance out this additional risk. (For example, the right star can inspires audiences to go out of their way.)

Location isn't the only important topic in the "Where" part of my analysis. One of the reasons that the exact theater is important is so you can determine if the size is adequate for your show's physical production (does the set fit?) and the show's financial needs. For example, putting

Wicked in a one thousand seat theater would have stressed the show's economics. There is a good reason *Wicked* is at the Gershwin, one of the largest theaters on Broadway.

Generally speaking, plays tend to be in theaters of about 1,000 seats or less (which are more intimate and can provide a better experience for the playgoing audience as well as the Actors). While more and more medium sized musicals have been produced in these play houses lately due to the unavailability of larger houses, most larger musicals aim to find theaters of 1,200 seats or more.

And yes, there is such thing as having a theater that is TOO big! Smaller, original shows might be better suited for a smaller theater. I'd much rather sell eight hundred seats in a thousand seat theater than eight hundred seats in a fifteen hundred seat theater. A half-empty house doesn't help word-of-mouth. Just because you have a larger theater with more seats, doesn't mean the show will sell out.

Finally, a show's artistic sensibility should be aligned with the venue. There is a reason that the Directors of Broadway shows usually tour the theaters under consideration before a contract is signed. The "artistic fit" can be as extreme as something like my Tony Award-winning revival of *Once on this Island*, which demanded the in-the-round Circle in the Square. Or it can be as subtle as the need for a front row close to the lip of the stage like at the Cort Theater in order to provide the most intimate experience possible for a new one-person show.

The *Where* question in this analysis is a combination of location, size and ensuring that the theater is the best artistic home for your production.

HOW MUCH

The last question in my investment checklist has to do with the nuts and bolts of the show's budget. After I assess the creative materials (the script, score, etc.), the budget is where I spend most of my time during the due diligence process. A show's budget is the foundation of the entire production. If it's not strong and sturdy, the show will fail, no matter how good it is.

When you receive your investment documents (which you should always look over *before* saying yes or no to investing in a show), you will also receive a complete budget of the show, which will have several components. That budget should include the following:

- A Production Budget
- An Operating Budget
- A Price Scale
- A Breakdown of Creative Royalties/Royalty Pool
- A Recoupment Schedule

Let's examine each of these items one by one in detail.. (A complete sample budget is including in our online appendix at www.TheProducersPerspective.com/appendix.)

PRODUCTION BUDGET

The Production Budget is usually in three parts.

As discussed, the first part of a Production Budget will consist of a summary of all of the expenses the show will incur leading up to opening night (scenery, costumes, rehearsals, audition expenses, etc.).

The second part will consist of a summary of advances, deposits and bonds needed for the production. These are the required expenses that the Producer expects to be returned and therefore do not need to be recouped, but still needs to be raised. For example, just like you might have a security deposit when you rent an apartment, a Producer needs to put down a security deposit when he or she rents a theater. And just like you expect to get that security deposit back when you vacate that apartment, so does the Producer when he closes his or her show.

The third part of a Production Budget will be a "reserve fund" or contingency, which is the amount of money that is set aside for budgetary overruns (changes in scenery, etc.) and, more likely, any losses that may be incurred during previews (the performances of a show on Broadway before the official opening) as the show gets off the ground.
Most shows, but especially new musicals, experience losses during previews just like any new business might experience losses during its first few weeks of operation. This is when the product is being discovered by the audience, and it can take a while for word of mouth to spread, especially if the show has not yet opened and reviews have not yet been published.

OPERATING BUDGET

The Operating Budget is the amount of money that it will take to run the show on a weekly basis, or the amount required to "keep the lights on."

As I stated in an earlier chapter, the most important part of a show's budget for you to review when you are considering investing or not is the Operating Budget. The details in the Operating Budget will give you the best insight into how high a financial hurdle the show has to jump over on a weekly basis in order to achieve profitability.

You're probably thinking that the correct way to find a good investment would be to only invest in shows with low operating costs. Well, if you rejected every show with high running costs you would have never invested in *Wicked*, *The Phantom of the Opera*, or *The Lion King,* which had some of the highest operating expenses in history at the time of their opening!

Think of it this way . . . if you have ever invested in real estate, you know that the smallest and cheapest property isn't always the best investment. The bigger properties, which are usually the most expensive, are often the most in demand, right?

The same is true for Broadway shows.

That's why you should never rule out a show just because it has a higher operating budget. The question you have to ask yourself in your due diligence process is whether or not you believe the show justifies a higher operating budget. Certainly, the spectacle of *Phantom of the Opera* and *Wicked* demand high costs, right? But a three person musical on a unit set with contemporary costumes that could be purchased off the rack at Saks which has the same running costs as *Phantom of the Opera* should raise some budgetary red flags.

Here is one of my favorite tips that I tell potential Investors to do when analyzing Operating Budgets in order to decide whether or not to invest in a Broadway show:

STEP ONE. When you are considering a show, ask yourself: *What show is currently running on Broadway that is most similar to the show that I'm looking at right now?* Is it similar in size, scope and audience appeal to *Kinky Boots*? *Come From Away*? Is it a revival like *Hello, Dolly*?

STEP TWO. Once you have identified one of two similar shows, take a look at the weekly box office grosses for that show. (Broadway shows publish their grosses on a weekly basis publicly which means there is a treasure trove of information available to investors. Subscribe to my blog at www.TheProducersPerspective.com to have the grosses emailed to you each week.)

STEP THREE. Calculate the average weekly gross of that show over a six month period.

STEP FOUR. Finally compare that average weekly gross to your potential investment's Operating Budget. Is it more? Consider that to mean your show is riskier. Less? That would make it less risky.

While not an exact science, this simple calculation will give you some context as to how much demand there is for this genre of show. Obviously, no two shows are alike, so use this as a general guide. But I find this process to be the closest you can get to determining if the Producer of the show has done a good job in creating a business model that is realistic and can be achieved. This simple step has saved me and my investors hundreds of thousands of dollars. I have said no to many shows because they've been budgeted like a *Wicked,* when they're actually more likely to have the ticket sales and length of a run like *Next to Normal*. (This process is similar of looking at "Comparables" in the real estate market, for you real estate Investors out there.)

PRICE SCALE

The Price Scale details the pricing strategy for the initial on sale of the show. This table will lay out the number of seats in each section of the theater (orchestra, mezzanine, balcony.) and the expected price for each of these sections, as established by the Producers and General Managers.

The Price Scale worksheet uses these prices and number of seats to determine a show's Gross Potential, or the maximum amount of money that can be made each week. One of the challenges of investing in the theater is that we have a fixed number of "product" (seats) that we can sell each week. Apple can always make more iPhones if customers keep buying them. But plays or musicals, as well as airlines, restaurants movie theaters or any "expiring inventory" industry can't make more product for a specific time if they've reached a certain capacity. That's why a show's Gross Potential is such an important figure to consider. If a show's Gross Potential is low and its Operating Expenses are high, the production becomes much riskier, because there is less potential profit you can earn each week. Less potential profit will result in a slower recoupment rate. The longer a show takes to recoup, the more chance for something to get in the way of that recoupment, like competition from a new show, a cast change, etc.

The potential Investor should also understand that the gross potential is just that . . . a gross “potential.” The figures on this sheet don’t take into account any discounts (group sales or single ticket discounts), and most shows offer discount when they enter the market. Conversely, these numbers don’t take into account any increases in ticket prices due to demand. In recent years, the Broadway industry has become very good at “variable pricing” (the practice of increasing prices over the original established price as a result of decreased supply and increased demand), and it is not uncommon for a popular show to gross *more* than its budgeted gross potential. In fact, that’s the goal!

Pricing now goes up and down so frequently that the price scale sheet in a budget has become more of a rough estimate than ever before. Expect these numbers to change constantly and don’t be alarmed if they do. A show with constantly changing prices is a sign of a show that is being run effectively, as the Producer is obviously trying to maximize income with the subtlest of changes.

> TIP! Ask your Producer how they will manage variable pricing since proper revenue management can have a major impact on the speed of a show’s recoupment as well as its long term profitability. Once we find a hit, we want it to make as much money as possible to give us more opportunities to make more theater.

ROYALTY BREAKDOWN

Some budgets will detail the composition of the creative team royalties (how much the writers, director, etc. are earning). This number is usually based on a percentage of the gross box office receipts, or more likely, a percentage of the weekly profit (with a minimum weekly guarantee). These amounts are often detailed in the show's Offering Documents. Don't be surprised if this sheet is omitted from your budgetary papers and instead a gross royalty figure is included on the Recoupment Schedule (described below).

RECOUPMENT SCHEDULE

Lastly, and most importantly, your budget will include a Recoupment Schedule. The recoupment schedule takes the most important numbers from the other Budget pages (Production, Operating, Price Scale and Royalty Breakdown) and puts them into a formula which calculates how long a show will take to recoup its capitalization at varying percentages of audience attendance.

This important spreadsheet will give you an estimate of how long it will take to get your original investment returned to you based on varying degrees of ticket sales. For example, it may state that if you sell out at full price (100% occupancy), the show will recoup its production costs in a 1,000 seat theater in 45.7 weeks. At 90%, it might be 51.2 weeks, and so on and so on, until the chart shows a "breakeven," or a percentage of the house where the operating expenses are met, but no profit is made. At "breakeven," a show can still operate, but a show would never pay back any of its investment to its investors.

(Confused? You won't be if you look at an actual recoupment schedule which you can get in our appendix at www.TheProducersPerspective.com/appendix.)

WHAT SHOULD YOU EXPECT?

It's not uncommon for a musical to need to sell 90% of its tickets at full price for a year in order to recoup its investment. While that may seem like a long time and a lot of tickets to sell in order to recoup, remember that the average run of a hit Broadway show is much longer than it used to be. So, while it may take a year for you to get your money back, the show could continue to run and pay profit for years after.

Plays, especially limited runs, have more restrictive recoupment schedules since they usually have to finite period of time to recoup. That said, because of their lower operating costs, it is possible for plays to recoup in a shorter number of weeks than a musical. *Lifespan of a Fact*, a brand new play that opened in the fall of 2018, recouped its investment after only about ten weeks of its sixteen week run! (This is a perfect example of the “smash and grab” that I described in the previous section.)

Remember, however, that for most shows, grosses *rarely* increase year after year. Because of competition, cast replacements, and other factors, most Broadway shows’ grosses decline from the first to the second year. So, if a show you’re considering investing in requires a high gross for an extended period of time, it might mean a riskier investment. (What does it take to increase grosses deep into a show’s run? A major publicity event, like a film or a Presidential visit, can have an effect. *The Phantom of the Opera* famously increased its grosses after its movie came out, which added years to the production’s life. See the blog I wrote that analyzed this case study in our appendix at www.theproducersperspective.com/appendix.)

Personally, I try to build a creative and economic model that provides for a recoupment at 70-75% of the gross potential in one year.

> TIP! Most Investors look at the percentage attendance of the house when examining a Recoupment Schedule. They'll say, "It breaks even at 50%. That's great!" What they fail to take into account is the size of the theater. When examining a recoupment schedule and the percentage of the house you need to sell in order to breakeven, make sure you ask yourself, "X% of what?" In fact, instead of looking at the percentage, I strongly advise you to look at the actual gross dollars that correspond with that percentage. Why? Well, 50% attendance in a 2,000 seat theater is a lot different than 50% in a 1,000 seat theater. It's the actual amount you need in dollars that is the most important, not the percentage. Remember what I said earlier . . . just because you're in a larger theater, doesn't mean you'll sell those seats. Only looking at the percentage can lead you to believe the show is more economically sound than it is.

Because our industry is so risky, we do not traditionally include any spreadsheets or projections that show potential profit (e.g. what happens *after* recoupment at 80% capacity.). I would like to see the Broadway industry begin to include these positive return scenarios, considering that other high risk industries like film do. However, *not* including profit scenarios does help manage investor expectations.

WANT TO CACULATE THE PROFIT ON YOUR OWN?

If you want to calculate an investment's potential profit, you can estimate the profit by using the "weekly profit" number at the bottom of the recoupment schedule for any of the various percentage capacities.
Here's what you should do:

STEP ONE. Divide the figure by two (remember, 50% of the profit goes to the Producers and 50% goes to the Investors). The result will be the amount of money allocated for the Investors at that capacity level.
STEP TWO. Multiply this gross Investor profit by the percentage your investment is of the total capitalization (e.g. $10,000 of a $1,000,000 capitalization would be 1%).

Please note this is a very rough estimation of profit, because after recoupment many expenses increase, including royalties, fixed fees, etc. Additionally, some creative and administrative team members may share in pre-investor profits (this is usually described in the Offering Documents) called "Net Profits." However, this back-of-a-napkin calculation will give you a rough idea of what you can expect to receive when your show is "in the money."

PUTTING THE FIVE W's (AND ONE H!) ALL TOGETHER

After I analyze all of the W's (and that important H) on a potential investment, here's how I aggregate it in order to determine a show's overall risk level.

After I am finished with my 5W's (and 1 H) checklist, I assign each category a score from 1-10, with 1 being the least risky and 10 the riskiest, which means every show has a potential total score of 6 – 60.

After I add all a show's individual category scores together (e.g. Who – 1, What – 8, Where – 9, When – 4, Why – 7, How much – 1 = 30), I instantly have a snapshot of how risky an investment is . . . based on my *own* risk factors, not someone else's.

This figure helps manage my expectations of a potential investment in a show. I have invested in shows with high scores (and therefore high risk) but because of this process, I've done so knowing that my chances of getting money back are unlikely. I therefore can come to terms with the "probability of profitability" before I make the investment and I can communicate this risk to my Investors. When a show has a high score, I often look for other potential returns that the show could deliver (awards, etc.) that are unquantifiable but may give me another reason to invest.

Shows with low scores (and therefore less risky by my algorithm) may encourage me to invest *more* money than I originally intended to invest, which would hopefully result in higher dollar returns.

All of this said, please know that the above system is not a perfect guide for your investment decisions, because of the many variables and factors in the theater industry that cannot be controlled. But I find it extremely helpful to be able to distill all of the information I have available on a potential investment down to a single number. And I hope it helps you too.

Remember, there is no "Yes" or "No" number. Use the risk-o-meter (or develop your own!) to determine how risky a show is and make the appropriate decision for you.

MONEY MANAGEMENT

One of the greatest strategies for investing in Broadway shows, or in any industry, is proper money management, or "diversification." Most financial advisors recommend diversification when investing in the stock market, and I recommend the same strategy for Broadway investing.

If you invest in the stock market (and I recommend you do . . . and then take a portion of the profits I hope you earn to invest in higher risk and higher return vehicles like Broadway shows), you would never invest all your money in just one company, would you? Instead, you'd invest in several different companies. Most likely you'd invest in some American companies, some foreign companies, some companies in the financial sector, some in the medical field, etc. In fact, the mutual fund industry was created to mitigate risk and make diversification easy for Investors. (A few Producers, including myself, have created "Broadway Funds" for those Broadway Investors seeking a similar way to mitigate risk.)

Let's use a more entertaining example to describe how diversification or money management can help increase your odds of making money in higher risk endeavors . . .

EVER GO TO VEGAS?

If you have ever been to Vegas or gambled in any casino, odds are you've said to yourself, "Ok, I've brought $500 to play with and if I lose that, I'm ok. And that's as far as I'll go on this trip."

Well, you wouldn't take that entire bankroll and put it all on one spin of the roulette wheel or one hand of Blackjack, would you? No. You'd want to make that cash last the whole trip, with the hope that your skill and luck would come around eventually, so you could gamble all weekend. By the middle of the weekend, you'd most likely be a smarter player, and make better decisions, thus increasing your odds of success (as long as you stay away from the free drinks!).

The same principles of diversification and money management that apply to the stock market and that casino in Vegas also apply to Broadway investing. While, as I've said, it's important to love each and every project you invest in, it's also very important to diversify into several different types of productions over a period of time. Remember, if on average, one out of five shows make money, you may need to invest in several productions before finding a winner.

One of the biggest mistakes that new Broadway Investors make is giving up on Broadway investing if their first investment is financially disappointing. Too often they swear off investing forever if their first show disappoints them financially, and they end up missing out on future opportunities. Usually, this happens when the risks of investing weren't properly explained to the investors beforehand, which is why it's essential to have proper expectations. If an investor understands the risks and practices proper money management, he or she can participate in multiple productions, and have a much higher probability of success.

As a first time Investor you may have to invest in a higher risk production before getting access to some of the more in-demand opportunities. That's why it's important you don't invest your whole bankroll in that first show, even if you love like it like it's your own child. Remember, you're investing in a fickle market that is subject to many arbitrary market conditions, and there are no "sure things." Make sure you always have some capital available (as well as some psychological capital to go back into the market after a show doesn't work out), so that if a great opportunity presents itself, you can take advantage of it. Or as I like to say, "Always leave room for dessert."

The first show I produced on Broadway was *13*, a unique musical with a score by Jason Robert Brown that featured an entire cast *and band* of teenagers. There wasn't an adult on the stage! (Side note - this is a key component of my producing style – to find shows that are exceptionally unique, and that have something on the stage <u>that an audience hasn't seen before</u> – because what hasn't been seen before gets talked about, and what gets talked about is what sells.)

Unfortunately, the show didn't recoup, partially due to the unfortunate timing of launching a family show in the fall of 2008, at the height of the financial crisis.

On the heels of that show, I was a Producer of *You're Welcome America*, Will Ferrell's one man show on Broadway that we discussed earlier. That show scored LOW on my risk-o-meter, indicating a much lower risk. I presented the opportunity to invest in *You're Welcome America* to my investors in *13* to give them the first chance at recouping some of their losses in *13*, which I expected to do very well.
Understandably, a few of my new Investors in *13* were skittish about investing in another project and passed on this new opportunity, instead of adhering to a consistent strategy. Unfortunately, they missed out on a show that would have recouped almost half of their losses in *13* because *You're Welcome America* was so profitable. And the show I produced

right after that was a money maker as well. And the show after that! And those investors missed all of them.

Investing in the theater requires a disciplined approach. I want my Investors to invest in multiple shows with me, and sometimes advise them to decrease their investment in one show so that they'll be able to invest in several, even if I'm not sure what the next show is. If you manage your money correctly, invest in a diverse set of productions (a new musical, a revival, etc.) and invest for the long term, you will have more opportunities to find a winner that recovers any losses you have incurred along the way.

Let's use a hypothetical example of how this might work over five shows, which is the average number of shows you need to invest in to find a winner.

Let's imagine you invest $25,000 in your very first show, SHOW #1. And unfortunately, that show is a complete loss. Of course, you'd be nervous about ponying up another $25,000 for SHOW #2. However, you like the show and the Producer and you go ahead and make a second investment. This show does better, but only returns 75% of its investment or $18,750. (Remember, just because a show doesn't recoup does NOT mean you will lose your entire investment.)

After two shows, you're down $32,250. You remember the law of Broadway averages and invest in Show #3 with another $25,000, which also returns 75%, bringing your total losses to $40,000 (Not $75,000 like you might think!).

Three shows, and you still haven't had a winner, and you're down $40,000. That's enough for most Investors to toss in the towel, but not you, especially since you've been to a few opening night performances and parties, learned about the marketing of Broadway shows, etc. So, you invest another $25,000 in SHOW #4 which does *worse* than the

previous two and you only get back 25% of your investment, bringing your total losses to date to $58,750.
Ugh.

And then a fifth show comes along, you put in another $25,000 . . . and FINALLY, you get a winner. And like so many Broadway winners when you hit, you hit big and it returns 350%. The total return for that show is $87,500, which pays for your previous losses and despite FOUR losing shows, you've got a positive return of $28,750.

And did I mention that the fifth show is going to tour? And be licensed?

Of course, this is just a hypothetical example, but it does demonstrate the reason why it's important to diversify your investments and remain disciplined with your strategy. Since Broadway investments can have explosive returns, it's not uncommon for one show to pay for many others . . . as long as you've continued to invest. Just be patient. It may take years to find the winner. (This is the same reason why certain hedge funds and private equity deals require your capital to be "locked up" for a number of years).

And remember, one out of five is the average number of shows that recoup. We now know that we have the tools and ability to beat that average and hopefully beat the market. So, we should be able to do better than the hypothetical example above.

IMPORTANT! If at any time during your Broadway investing experience you are no longer comfortable with the potential of losing your entire investment, you should stop immediately. One out of five is the average, but every investment has the potential to be a complete loss. Remember, flipping a coin has 50/50 odds, but it is possible to get ten "tails" in a row! Invest wisely and only with capital you can afford to lose.

Diversification not only helps increase potential returns, but when you invest in multiple productions, you'll get perks with each production. As I told an Investor who I advised to split a $100,000 investment into two $50,000 investments in two shows instead of investing the entire $100,000 in one production, "Why go to one opening night when you can go to two?"

INSIGHT FROM ACTUAL BROADWAY INVESTORS ON SUCCESSFUL STRATEGIES

The following are answers from real Investors to questions regarding their strategies for choosing what they invest in and what they avoid.

Q: What is the most important thing you look for when considering an investment in the theater?

Investor #1: "That I thoroughly enjoy the show. I go with my gut. Does it have a great message? Does it make people happy? Is it funny? What are the financials? Who is the cast? What is its pre-Broadway history? Is it commercially sellable? They are all factors that go into my gut assessment."

Investor #2: "People, trust, and marketability. The people producing, directing, and acting in the show must be excellent, trustworthy, and authentic. Trust is key, from the transparency of the reporting, the willingness to share bad news, and openness about the process along the way. Finally, the marketability is key. We now must be able to talk about a show in 140 characters of a Tweet or five lines in a text message—sent from the lobby during intermission. If we can't describe it well in those formats, it won't sell!"

Investor #3**: "**Connection to the project whether by way of the music or book and a belief that the project will be viable. I invested in a show that was not ready when we started previews.

The key is to have a creative and production team that will do surgery, if needed, to evolve, fix, and sometimes even close the show if it is not ready for the white lights of Broadway. It is a sporting business for us. We want to win. But we really want to love the process along the way."

Investor #4: "I invest only with a Lead Producer I trust, and I know. And I choose carefully, look at the numbers, and then go with my heart and my gut. I am about the music. So, if the score is wonderful, then you've got my attention."

Investor #5: "I want the numbers to make sense (but not be overly optimistic). As a general rule, I like to see proven talent/creative attached. I also want to have a personal interest in the show/material."

Investor #6: "I look at a potential investment in two ways. First, do I think it is commercially viable and what do the numbers look like in order to determine if there is a decent chance the show will recoup? Secondly, and equally important to me, is, does this project speak to me? I want to have passion for a project, especially considering the probability of shows not recouping fully."

***Investor #7*: "**Lots of factors go into my decision to invest, including an affinity for the material, what the show brings to the community, the creative team, as well as the detail and thoroughness of the information provided to the Investor in the offering papers. But ultimately, the decision always turns on one factor, the Producer with whom I am investing. As a limited partner or LLC member, investors have no actual control or input into the process and are totally dependent on the Producer to keep them updated on the production. As a result, total faith and confidence in the Producer, your interface to the project, is critical. I look for individuals who cultivate personal relationships, not just take money. I look for individuals who are realistic in the explanations of the risks because I know them very well and can tell when I am being snowed. I look for individuals who are respected in the community and with whom other producers are willing to collaborate. And finally, I look for an individual who I know will be transparent and tell me the good news and the bad. I now work with a limited number of producers who I got to know over a period of time, and with whom I have had nothing but positive experiences, even when the entire investment was a loss. I had one very bad experience with a Producer, and ultimately, I believe at least some of the signs were there, and I could have avoided the situation entirely if I had done a better job on my homework."

***Investor #8*: "**There are many factors that play into my decision, but the most important one?! The person I'm investing with is more important to me than the actual project. If I believe in the Lead Producer, there is a stronger chance that I will invest because I believe in the philosophy to which they adhere. I have made investments in projects I was excited about only to learn that I get no weekly feedback on the project, no updates, and no perks with the investment. Those experiences have changed the way I invest. If it's not fun and it doesn't include an experience, I'm not interested. Bottom line."

***Investor #9:* "**I consider one question: am I truly excited about the prospect of seeing this show live on stage? For example, when I heard about *Somewhere in Time*, I knew that I wanted to be a part of it because I loved, loved, loved the movie and could picture the characters singing their hearts out."

***Investor #10:* "**I look for an opportunity to invest in art and artists and good work. It's not about looking for a quick buck. (I would clearly be barking up the wrong tree if that were the case.) Do I kick myself for not investing in that blockbuster hit? Sure. But that takes tens of millions of dollars, which is a bit out of my league. The only thing I may regret is an opportunity to earn back profits from that blockbuster, which I could then pump back into a smaller production. Maybe I'm naive, but I'm just hoping that one of those smaller works has a chance to hit it big too. I never risk more capital than I can afford to lose if the whole show went bust. This, too, helps me sleep at night."

QUIZ!

1. In general, what type of Broadway show has the most financial upside?
    a. New Off Broadway Musicals
    b. Broadway Musical Revivals
    c. New Broadway Musicals
    d. New Broadway Plays
    e. Broadway Play Revivals

2. How many of the ten longest running shows in Broadway history featured stars in their original casts?
    a. All of them
    b. 20%
    c. None of them
    d. 50%
    e. 80%

3. What part of a show's budget puts all of the key figures in one place and calculates when you could receive your money back?
    a. The Production Budget
    b. The Price Scale
    c. The Recoupment Schedule
    d. It isn't in the budget. You have to figure it out on your own.
    e. The Operating Budget.

ANSWERS: 1(c), 2(c), 3(c)

Chapter Five

Getting Started

Congratulations learning the nuts and bolts of Broadway investing! If you've read this far, you now understand the risks involved with investing in Broadway, have more of a knowledge of the mechanics of investing, and, most importantly, you have strategies and tools to help you mitigate the risks and improve your results in an effort to beat the market.

If you're still excited about the idea of Broadway investing, despite the 193 times I've told you how risky it is, it's now time for you to make your first investment.

But how?

Many people like you get want to invest, but don't know how to get started, since Broadway Producers don't advertise their investment opportunities and in most cases are legally prevented from doing so.

In this chapter, I'll give you some advice on getting your foot and checkbook in the door so you can make your first investment and participate in the fun and potentially lucrative world of Broadway investing.

First, to invest in a Broadway show, you have to "know someone." It's not possible for an investor to open an online investment account and buy shares in the next Lin-Manuel musical. If only! Broadway offerings are private, so you must find a connection to make an investment.

So, what do you do if you don't know anyone? That's easy. <u>You get to know someone.</u> It's not as hard as you think, but you do have to be proactive.

WHOM DO I INVEST WITH?

Broadway shows are similar to Private Equity opportunities or some Initial Public Offerings. IPOs and Private Equity opportunities can be highly sought after, and to get an opportunity to invest in such an offering, you usually have to have the right connection. (Not everyone was given a chance to invest in Uber or Facebook before they became Uber and Facebook.)

Generally speaking, there are two ways to get investment access to a Broadway show:

- Through the Lead Producer
- Through a Co-Producer (or Bundler)

(I'll discuss Co-Producers and Bundlers including their function, responsibilities and how to become one, in the next chapter, *Advanced Strategies*.)

You already know that the Lead Producer is the individual, or group of individuals, who are in charge of the show. The buck stops with him or her. They make the final decisions and have the most intimate knowledge of the show itself, as well as the financials.

That's why, whenever possible, it's more advantageous for you to invest directly with the Lead Producer, rather than through a Co-Producer or Bundler.

This doesn't mean that you should NOT invest with a Co-Producer if that opportunity presents itself. First, this may be the only access you have when you start investing, since Lead Producers are often more difficult to find and start a relationship with. Second, there are some fantastic Co-Producers out there who can help you learn more about Broadway investing. Often these Co-Producers started in the business as Investors, just like you, so they can be very helpful as you begin to invest in the industry.

But, if you have a choice, I always recommend you invest directly with the Lead Producer first, since you'll get information straight from the source, and you'll develop a relationship with that Producer for future projects. (Guess who some of my peers got the option to invest in *Hamilton?* By doing other shows with the same Producers, including some that weren't successful . . . but they certainly don't mind those losses now!)

<u>HOW DO YOU FIND A PRODUCER?</u>

There are several easy ways to find Producers to invest with. A few minutes on Google, Facebook or LinkedIn will yield a number of results. (Again, just make sure you identify whether or not the Producer is a Lead Producer or Co-Producer when you begin discussions about projects, as sometimes it's not always clear.)

Since one of the most important factors of successful Broadway investing for first timers is to make sure the show you're investing in is something you will enjoy and be proud of, I encourage new Investors to seek out Producers who have similar tastes, values and expectations for their shows.

That's why I suggest my . . .
FOUR STEP PROCESS TO A FIND A PRODUCER TO INVEST WITH!

STEP ONE. Go see lots of shows.

Tough homework, huh?

STEP TWO. When you like a show, flip to the title page of the Playbill and look at the Producer billing ABOVE the title of the show (and below the theater owners).

STEP THREE. Circle the names at the very top of the Producer billing. Sometimes there will be one name. Sometimes a few. But the Producers on the top line are usually the Lead Producers.

STEP FOUR. Contact the Lead Producers through email, letter, Facebook, phone call, etc. and say you recently saw their show, enjoyed it, and would like to be added to their list of potential Investors.

And that's right, I did say "call," by the way. It's more than ok to call a Producer's office, especially to say you have an interest in investing! This is not the time to be shy. If the Lead Producer won't or can't take your call, you can always tell the assistant that you'd like to be added to a list of future Investors. I don't know of a Producer's office in town that won't take your information if you say you're interested in investing! After all, as I said when I accepted the Tony Award for *Once on this Island*, "Investors are why Producers have a job!" And remember, raising your hand and saying you're interested, doesn't mean you have to write a check.

Complete this four step process a few times over, and you'll have plenty of opportunities to choose from in short order.

And by reaching out to a Producer of a show you enjoyed, you will know that you're investing with someone who has similar theatrical tastes. And just because you're reaching out, doesn't mean you're obligated to invest. Reaching out and getting on a list could get you future opportunities, an invitation to a reading of a new show, etc.
I'd also recommend checking out the Producer's prior experience on The Internet Broadway Database (www.IBDB.com). Not only will you get

further information about the Producer's history and taste from the shows he or she has produced, but you should also be able to determine the Producer's recoupment rate. While IBDB doesn't have recoupment statistics, if you google the name of the show and the word "recoup," odds are you will see a press release about the show recouping, or you won't. Since most commercial Producers usually scream about their recoupment in press releases, if you don't find a release about the recoupment, you can bet that the show did <u>not</u> recoup. It won't take you too long to determine if that Producer is beating the market. While this is not a scientific way to determine a Producer's financial success rate, it is as close as one can get without inside information.

And don't hesitate to ask a Producer directly about his or her success rate!

When talking to a Producer for the first time, remember that you will be a brand new Investor for that Producer, and the most exciting opportunities from that Producer (the ones with lower risk on the risk-o-meter) may only be offered to the Producer's family of loyal investors first. (You'll benefit from this someday.) The opportunities you are given to new Investors may be riskier. This is important to know when you evaluate that opportunity. If you go ahead with the investment, you want to make sure you will get access to future opportunities with the Producer. Sometimes, I've invested with a Producer knowing that he was producing a project in the future that I was interested in. You can bet I made it a condition of my investment in the first project to get access to that next one!

> TIP: When you make an investment with a Producer, ask for a commitment (in writing if possible) that you'll have access to the Producer's next projects.

Some of my most loyal Investors have been people I've received emails or letters from after they have seen a show of mine, or after they heard me speak at an event. They responded to something I've produced or said, and they reached out because they realized that we have something in common. And now, when I have something that appeals to them, they invest.

Because the relationship begins on common ground, it lasts for a long time. Those are the types of relationships you should seek out when you begin investing.

MAKING SURE YOU GET IN BEFORE IT'S ALL GONE

Because investing in Broadway shows has become such a popular alternative investment, thanks to the recent string of big returns from shows like *Hamilton, Dear Evan Hansen, Come From Away*, not to mention *Jersey Boys, Beautiful*, etc. many shows have completed their financing earlier than shows did a decade or so ago.

That's why it's important to raise your hand as quickly as possible when you hear about a show that you're interested in, and also to make sure that you are one of the first to hear about those shows.

Just like good Investors in the stock markets read publications like *The Wall Street Journal* and *Investor's Business Daily*, you should scour the Broadway "trades" to know what's coming to Broadway before the financing is closed.

Of course, I recommend *The New York Times* Arts and Leisure section for Broadway news, but I'd also recommend our niche sites like Playbill.com or Theatermania.com, which post more articles about developing shows. For example, I am developing a musical based on the *Vacation* movie franchise as well as a musical based on the life of Joy Mangano (subject of the movie *Joy*). When I acquired the rights, we sent out a press release, which was picked up by all of the trades and several national publications as well, but *not* the New York Times. Several people saw the articles and emailed me about their interest in investing. That's the kind of quick action it takes in this era of Broadway investing in order to ensure you get the access to the projects you want.

TIP: Check out the trades to be the first to know about projects!

DON'T FORGET TO ASK FOR THE MATERIALS!

When you reach out to a Producer and express interest in a show, or after you attend a reading, ask for any materials that the Producer has in addition to the financial package and offering documents.

For a musical, a script and demo of some of the music will usually be available. For a play, you should be able to read a script. And sometimes, you'll be invited to see a reading or a workshop. Look at these materials and take readings and workshops seriously when evaluating the opportunity. You'll have to use your imagination when considering what the show will become when it is fully produced. But, you're a theatergoer, right? Look for material that would make you want to go see it! If you invest in what you respond to, you can't go wrong, even if the show doesn't work out financially. And if you like it, odds are others will too.

TO GET STARTED, YOU HAVE TO GET STARTED

If you've gotten this far in this book, then investing in a Broadway show is something you serious about. The biggest tip I can give to those interested in investing who want to get started is . . . get started. A big mistake that first time Investors make is that . . . *they don't become first time Investors!* They know that investing in Broadway show is risky, and despite their desire to get involved, they sit back, waiting for the perfect opportunity. Recently a potential Investor said to me, "I'm not interested in that show, but when you have a *Hamilton*, let me know."

Ha!

I promise you, the Producers and Investors of *Hamilton* didn't know they had *Hamilton* until well after they made the investment.

This potential Investor's comment is like saying to your stock broker, "Hey, when you have the next Amazon, let me know and I'll give you some money." (Funny thing is, I had the opportunity to invest in Amazon in 1997 after it went public at $49 a share, and my broker at the time though it was too expensive. A $10,000 investment would be worth over $300,000 today. #Oops. #IBlameTheBroker.)

You will never know when you have the next Amazon, Facebook or *Hamilton* until after you invest.

(FYI, I deleted that gentleman's contact information after he made that *Hamilton* comment, because I knew investing in Broadway was not for him. Frankly, walking down the street might not be for him because he was looking for a guarantee that only amazing things would happen with everything he did and that's just not how life, or investing, works.)
So yes, find a project and a Producer you like and make sure the show's economics are consistent with your goals . . . and then jump in. Make that first investment small, so if it doesn't work out, you aren't scared

away. But remember, the way to learn is to play the game. And the one guarantee I can make about investing is that you will never be able to invest in the next *Hamilton* without investing in the first place.

QUIZ!

1. Which of the following is an inappropriate way to contact a Producer?
    a. A letter
    b. A phone call
    c. A LinkedIn message
    d. A note left at the stage door
    e. None of the above

2. If you had a choice, which of the following should you invest with?
    a. General Manager
    b. Co-Producer
    c. The Star
    d. Lead Producer
    e. None of the above.

3. Where can you hear about new shows that might be looking for investment?
    a. The New York Times
    b. Playbill
    c. Ken's Blog
    d. Your class reunion
    e. All of the above

ANSWERS: 1(e), 2(d), 3(e)

Chapter Six

Advanced Strategies: Before We Begin

I wasn't planning on including this section in this book.

But the more Investors and potential Investors I speak to, the more I am asked about additional ways to maximize possible returns, both financial and experiential.

Therefore, I am including a description of three of the most common advanced investment strategies on Broadway.

Please note that these strategies can involve greater risk, a greater investment of capital (yours or your network's), or both, so please make sure you perform proper due diligence before proceeding with any opportunity presented to you and remember that Broadway is a high risk investment.

In addition to a lawyer, accountant or other trusted advisor, I strongly recommend you speak to an experienced consultant in the Broadway industry who can give you objective and unbiased advice on the project and financials before you proceed with any of these strategies. If you need a recommendation of someone to talk to, please email me at ken@theproducersperpsective.com and I'm happy to point you in the right direction. I want to make sure you are making an educated decision when considering these options. And now, the Advanced Strategies section!

Chapter Seven

Advanced Strategy #1: "Co-Producing"

How would you like to earn a higher percentage return on your investment, be eligible to win a Tony Award, attend marketing meetings, and be able to tell your friends and family that you're a Broadway Producer?

And what if I told you it was possible to get all of this and more without investing any of your own money?

Interested?

I thought so.

Welcome to world of Co-Producing on Broadway, which is a way for the more advanced Investor to get more involved in the actual production of shows, get access to meetings and rehearsals, meet cast members, earn money without risking their own money, and more.

Co-Producing is what many of my Investors look to graduate to after they invest in a few shows, as it gives them more of a sense of inclusion and participation in the production of the art, rather than just being a passive Investor. These Investors realize that investing in Broadway is a high risk endeavor and may result in a loss of capital, so many are actually willing to risk more capital to insure they get a better experiential return, which Co-Producing can provide.

Because there are many other ways to get an ROI than in cash.

But I'm getting ahead of myself. Let's start at the beginning.

As we've discussed, on Broadway there are two kinds of Producers:

1. Lead Producers
2. Co-Producers

As you now know, the Lead Producer is the individual who originates the production (conceives the idea, options the script, commissions the writers, etc.) The Lead Producer lights the fuse on the production, or as I like to say when I speak to corporations and groups about entrepreneurship, the Lead Producer "serves the tennis ball." He or she starts the game and keeps the volley going, all the way from the origination of the idea to the opening night. To use a corporate analogy, a Lead Producer is like a CEO, or a Chairperson of the Board of a major corporation.

And just like a corporate Chairperson has board members, so does a Lead Producer. And yep, you guessed it, in Broadway terms, those "Board Members" are Co-Producers.

These Co-Producers are major Investors (or aggregators, bundlers, etc. as I'll define below), and therefore have earned the right to sit at the table with the Lead Producer, and offer opinions, suggestions. They can help influence the journey of the production and can be some of the Lead Producers' closest advisors.

That said, a Broadway show is not a democracy. The buck will still stop with the Lead Producer and while the best Lead Producers in town will listen to every Co-Producer's opinion on a subject, the final decision will come down to that Lead Producer. Some Lead Producers will put a debated issue up to a vote. However, it is important to remember that at the end of the vote, the Lead Producer may still decide to go a different way. Unlike some corporate structures, all decisions are up to the Lead Producer and there is no majority rule.

THE HISTORY OF THE CO-PRODUCER

While Co-Producing has always had a place on Broadway, modern-day Co-Producing was born in the early 2000's.

In the early days of Broadway, there were only one or two names of Producers above the title on a show's poster, or on the title page of the show's Playbill. For example, the original production of *Gypsy* had two Producers billed above-the-title. *West Side Story* had three. *The Phantom of the Opera* has two.

But now it's common to see ten, twenty or sometimes even more names above the title of a Broadway musical. *Kinky Boots* has twenty-two names above the title!

What happened?

First, Broadway shows became more expensive. Raising $10 million to $20 million is a lot of work and a great deal of risk. That's why Lead Producers began to enlist the help of larger Investors to help fund a greater percentage of the capital required to produce a show. This meant more risk for the larger Investors if they were investing the capital themselves or more work if they were raising the money from their Investors. So, as a way of enticing the larger Investors to take this risk or do this work, Lead Producers began to look for other perks to sweeten the pot and help mitigate the risk of the larger investment.

The most valuable perk available was "billing," or the Investor's name listed above the title with the Lead Producer. Why was this perk the most valuable to offer? Because when your name is above the title, you become eligible for a Tony Award. If your show is nominated, and you are listed above the title of a Broadway show as a Co-Producer, you'll receive a nomination plaque and a nice "Tony Nominated" credit for your resume and bio. And yes, if your show wins, you can receive a Tony Award of your own, and perhaps be able to appear on stage during the Tony Awards telecast.

For so many, the potential of a nomination and/or award is a priceless "return on investment" and is worth the additional risk. This is why more Lead Producers began to offer above-the-title billing to Co-Producers, and more Co-Producers began to accept it.

While there are many in the industry who have looked down on the number of names above the title of modern musicals, I think it's important to remember that it's because of these Co-Producers that many shows have been produced. And without them, they may not have happened at all!

For example, one of the first shows that got a lot of attention for featuring so many names above the title was the original production of *Spring Awakening*. Because that show had challenging subject matter, there was a concern that the show was not "commercial" enough for the Broadway audience. That made it a risky to show to invest in and therefore a difficult show to raise money for. That's why the Lead Producers offered very low thresholds to be an above-the-title Co-Producer. While some folks in our business put their nose up about the low "entry point" to be a Broadway Producer (all of the Co-Producers won Tony Awards), I'd argue that having that many names above the title of a show is a small price to pay if it means a great piece of theater like *Spring Awakening* gets a chance to open on Broadway. (And since I produced the revival in 2015, I'm very thankful that the original Lead and Co-Producers made this show happen!)

Additionally, if a Lead Producer is able to "subcontract" out the financing of the show to other Co-Producers, that gives him or her more time to work on the creative development of the show, the marketing, advertising, casting, etc. Broadway Producers are among the few types of producers in the entertainment industry who are responsible for raising money. Studio Film Producers, TV Producers and Record Producers don't raise money. They are hired to produce. Broadway Producers hire themselves, therefore part of their job is to raise the funds necessary to launch the production. I often say if I didn't have to raise money for my shows, I'd be a better Producer, because I'd be able to concentrate on the two things that Producers should focus on:

1. Making the show better.
2. Selling the show better.

Co-Producers help take some of the money-raising responsibility away from the Lead Producer which allows the Lead Producer to spend more time working on the show's elements that will affect recoupment, while at the same time giving Co-Producers more of an involvement in the production and giving them a preferred rate of return.

WHAT DOES IT COST TO BE A CO-PRODUCER

When you express interest in being a Co-Producer on a Broadway show, you'll be given a list of amounts or thresholds required for Co-Producer billing. (I've included an example of a Co-Producer Offer Sheet in our online appendix at www.TheProducersPerspective.com/appendix.)

Just like the cost of an investment Unit is arbitrary, there is no set or standard level to be a Co-Producer on Broadway. Every show is different, and the Co-Producer levels are set by the Lead Producer.

The levels depend on a number of factors, including:

- The risk of the production (usually the higher the risk, the lower the threshold)
- The style of the Lead Producer

But take a moment, and ask yourself . . . what do you think you would need to invest or raise in order to be a Co-Producer on Broadway?

$1,000,000? $750,000? $500,000?

Yes, all of these are customary levels of Co-Producing on Broadway. But it is not uncommon to see some Co-Producing options for as little as $350,000, $250,000 or even $150,000. (Usually, the lower thresholds are for plays or for shows that are considered higher risk.)

> TIP: Remember, when something seems "too good to be true" (a very low threshold) it often indicates an extremely high level of risk. Like any factor you evaluate, a low threshold shouldn't mean you should definitely avoid the production (See www.TheProducersPerspective.com/appendix for an article about the low thresholds offered on *A Gentleman's Guide to Love and Murder* that turned all the Co-Producers into Tony Award winners *and* the show also recouped*)*. In fact, just like I like to accept small investors and investments on my productions, I often set low thresholds for Co-Producing to allow more people, especially those just starting out, a chance to get involved. However, in some cases, a lower threshold may be a hint that there is additional risk involved in the production. I recommend asking your Lead Producer how they set their thresholds.

YOU DON'T NEED YOUR OWN MONEY TO BE A PRODUCER

One important thing to remember when you are presented with a threshold for Co-Producing that may seem higher than you want to invest on your own, is that in most cases you have the opportunity to raise some or all of that amount from other Investors. Co-Producers can either invest or "cause to be invested" (i.e. raise money from other Investors) the amount required for Co-Producer status. So, if you were planning on investing $25,000 in a production and the threshold for a Co-Producer was $250,000, you would need to raise the other $225,000 (for example, find nine other investors like yourself at $25,000 each) to earn the Co-Producer title.

WHAT DO YOU GET AS A CO-PRODUCER?

There are many different perks afforded to Co-Producers. The two most popular reasons individuals Co Produce is for the "billing" and for the additional financial incentives.

BILLING

As stated above, billing refers to your name above the title of a show. Open any Playbill for a Broadway play or musical and you'll typically see many names above the title. As a Co-Producer on Broadway, that's where your name would be.

There is a hierarchy within that list of Co-Producers. The more you invest or raise, the higher your name should appear among the list of Co-Producers. I list my Co-Producers on my Broadway shows by order of money invested or raised from highest to lowest. The positions closest to the Lead Producers are the most valuable.

In addition to billing, Co-Producers are traditionally afforded a reasonable length bio in the Playbill, which is a chance for the Co-Producer to list his or her credits, thank his or her spouse, or even subtly market his or her day job!

WHAT NAME DO I PUT UP THERE?

Many first-time Co-Producers think they have to put an official company name above the title of the show (e.g. the name of an LLC they form). But you can actually use any name you want! You can use your personal name, the name of a company, your daughter's name, or any name you'd like, as long as it is approved by the Lead Producer. The name you use in billing does not have to be the name of your investing entity, LLC, etc. I'm listed as Ken Davenport on all of my shows, although that is not the legal organization that produces the show. It's just the name I want people to think of when they think of who produced the show.

TIP: If privacy is a concern, I'd strongly suggest you do NOT use your own name. Once your name appears above the title of a production on Broadway, you can expect other people raising money to track you down and offer you chances to participate in other shows. This may be attractive to some of you and may be a reason *for* putting your name on a show in the first place! However, others may want to remain private to avoid these kinds of solicitations. In those cases, I'd suggest you create a company name to receive the credit. But DO take the credit under some name, as it does mean potential awards nominations, wins, etc. as we'll discuss below.

WHAT ABOUT THOSE SLASHES?

On some title pages you may notice what the industry calls "slash" billing or several names listed together separated by a slash. This type of billing is not available on all shows and is only allowed subject to the approval of the Lead Producer. In exchange for shared or slashed billing (e.g. Ken Davenport/Tracy Weiler/McKenna Davenport), the threshold to become a Co-Producer is usually less than that of single name billing. For example, in the slashed example with my name and my wife and daughter's name above, a single name Co-Producer title (e.g. Ken Davenport) may have required me to invest or raise $500,000. But to be one of a slash of three names, I might have only need to invest or raise $175,000, and Tracy Weiler and McKenna Davenport would also only be required to invest or raise $175,000. In this example, all three names are given credit (although shared) and the Lead Producer ends up with $525,000, which is $25,000 more than he or she would have received from one name.

Slash billing was not looked upon very fondly by some of Broadway's elite when it first started to appear in Playbills, but it has become more accepted as a way to allow Co-Producers to diversify their investments and participate in more productions. And again, if it helps get shows off the ground that might not normally have gotten to Broadway, then I believe a slash is a small price to pay.

TIP: You may not see slash billing opportunities on the Offer Sheet for Co-Producers, but don't hesitate to ask if there are slash options available when you are discussing Co-Producer opportunities. Just like a Lead Producer has the option to take fractional units but doesn't advertise it, he or she usually has the opportunity to give you deals that are not on the Offer Sheet.

FINANCIAL INCENTIVES

When Investors invest larger amounts or raise larger amounts, they are doing two things:

1. Assuming greater risk.
2. Making the Lead Producer's job of raising money easier.

That's why it is common for Lead Producers to incentivize Co-Producers with billing, but also enhanced financial returns. It only makes sense that if you're risking more money, you should get a better financial return, or if you are raising money, you should receive compensation for raising that money.

Generally, it is not legal to compensate anyone with a fee for raising money, like a Finder's fees or commission, unless that person is a registered "Broker Dealer" with the SEC. Although I use the term "raise money" when discussing the activities Co-Producers, actually the Co-Producer is merely "introducing" potential Investors to the Lead Producer who retains the discretion to accept or reject the proposed investment. So, the actual compensation that is paid to the Co-Producers is for this 'introducing" of potential investors.

Further, all compensation comes out of the Lead Producers financial entitlements. In other words, none of the operating proceeds from the production are used to compensate Co-Producers and no Investor's return is diminished as a result of these arrangements.

For their involvement in the production, Co-Producers may expect to receive:

1. A heightened share of Post Recoupment Profit
2. A participation in the Lead Producer's Weekly Royalties/Office Fees

PROFIT

Profit is the most common type of compensation for Co-Producers.

Compensation for Co-Producers is paid out in what we call "Adjusted Net Profits" or a portion of the profits of the production based on how much money the Co-Producer invests or raises.

IMPORTANT: These profits are "post-recoupment" dollars. Money is not paid to the Co-Producer until the Investors have recouped their original investment.

While the amount the Co-Producer may anticipate in exchange for their investment is a percentage of their amount attributed to them, this supplemental amount is more commonly referred to as a "1 for X" deal. For example, for a $500,000 investment, a Co-Producer may receive a "1 for 4" deal.

What a "1 for X" deal means is that for every X dollar that the Investor receives in profit (post-recoupment), the Co-Producer will receive one dollar. One dollar for X dollars. Make sense?

Probably not. It's confusing, I know, so allow me to use a hypothetical example to help demonstrate this important concept.

MEET OUR CO-PRODUCER, JANE!

Jane, a Co-Producer, raises or personally invests $1 million of a $10 million Broadway musical. For this investment of 10% of the entire capitalization ($1 million of a $10 million production), Jane is afforded a "1 for 2" deal.

The show recoups and Jane and/or her investors receive their one million dollars back. Over the next four weeks, the show profits $200,000. The Producer and General Manager feel confident enough in the size of the reserve that they decide to process a distribution of the $200,000.

Now, as you recall, after recoupment, any profit is first split 50/50 between the Investors and the Producers, so this $200,000 is first split in half: $100,000 for the Investors and $100,000 for the Lead Producer.
Got this so far?

Since Jane invested or raised 10% of the total capitalization, She and/or her investors would receive 10% of the $100,000 of Adjusted Net Profits flowing to all Investors or $10,000 for their investment.

But what about Jane's additional "1 for 2" profit deal for being a Co-Producer?

Since the Investor share is $10,000, and since Jane is getting a "1 for 2" deal (which means for every $2 the investor receives, Jane will receive $1 as a Co-Producer), you simply divide the $1,000 by 2 to see what Jane would receive for being a Co-Producer, which in this case is

$5,000, paid to her by the Lead Producer out of the Lead Producer's share of the Adjusted Net Profits.

In percentage terms, this means Jane gets a 50% "kicker" on the Adjusted Net Profits payable in respect of the capital contribution she made.

Now, if Jane *raised* the entire $1 million and did not invest any of her money, she would still receive the $5,000 Co-Producer kicker, and her Investors would still receive $10,000 from the investor side. This is an important concept to understand as it demonstrates how a Co-Producer can earn significant revenue by producing Broadway shows *without* putting his or her personal capital at risk. In this example, if Jane ALSO invested the entire $1 million, she would receive $10,000 from the Investor side and $5,000 from the Producer side, for a total of $15,000.

The $5,000 Co-Producer profit is deducted from the Producer's 50% share of the profits. So, when a Lead Producer cuts a "1 for X" deal with a Co-Producer, he or she is giving up a portion of his or her own potential personal profit in exchange for the Co-Producer making his or her job easier. (In this example, if Jane was the ONLY Co-Producer than the Lead Producer's profit in this profit cycle would be . . . any idea? $100,000 - $5,000 or $95,000.)

Obviously, the lower the number of X in a "1 for X" deal, the better for the Co-Producer. This number, like billing and the threshold for becoming a Co-Producer, is entirely up to the whim of the Lead Producer, although, again, it is usually based on demand, appetite for the investment and other factors.

But for average Co-Producer deals, you can expect deals between 1 for 3 and 1 for 7. 1 for 2 deals are usually reserved for more significant capital, or very early financing (see Advanced Strategy #2!) And for

Investors who put in the very earliest and riskiest money, a return as high as 1 for 1 is possible, i.e., a potential doubling of the standard profit participation. (See the upcoming chapter!)

TIP: Again, under a standard Broadway financing deal, it is clearly in appropriate for a Lead Producer to pay "Finder's Fees" or any kind of compensation directly related to the raising of money other than to registered "Broker Dealers," and on a disclosed basis (and this never happens). If someone offers you cash in advance to provide an investment or to find Investors, be very careful, as it is not customary and signals that the Producer is either inexperienced, desperate, or both.

ADDITIONAL PERKS

While billing and financial incentives are the two primary reasons Co-Producers invest or raise larger amounts of capital, there are a number of additional perks you should look for and *ask for* when negotiating your Co-Producer agreement.

OPENING NIGHT TICKETS

Co-Producers are often afforded more opening night tickets for themselves or for their Investors. Since attending the opening night performance and party is such an important reason people invest in the theater, opening night tickets are huge perks to be able to offer to potential Investors when raising money. Make sure your Co-Producer agreement guarantees tickets for yourself *and* for your Investors. Usually, the Lead Producer will give you a pair of opening night tickets for each investment of a certain amount. For example, if you raise $250,000, a Lead Producer may give you a pair of tickets for every $50,000 Investor plus at least one pair for yourself.

ADDITIONAL COMPANIES

Just like an Investor, as a Co-Producer you should be afforded the right to invest in or raise money for additional companies of the show produced by the Lead Producer, *ideally on the same terms and conditions* (financial deal, billing, etc.) of the Broadway production. Just like investing, this can be your chance to parlay your original investment into several successful investments if you find a winner. These opportunities are what can erase the losses of previously unsuccessful investments, so it's important you have this right. But do note . . . on "hot" shows, Producers are increasingly not committing to the original investment terms, so do read this section of your agreement carefully.

ACCESS TO REHEARSALS/TECH/PREVIEWS, ETC.

While this is sometimes difficult to negotiate, if attending rehearsals, etc. is important to you, make sure you ask the Lead Producer if it is possible to watch the process before performances begin.
You can also ask for free tickets to previews, or early performances, so that you can watch the show develop (watching shows change during previews is one of the most exciting parts of the process of developing a new show). I encourage my Co-Producers to attend as many performances as possible to enhance their education and experience.

GET A FAVORED NATIONS DEAL

The most important language you must ask for in a Co-Producer deal is a "Favored Nations" clause, which legally requires the Lead Producer to give you the same terms and conditions given to any other Co-Producer *at or below your level of investment.* (If someone invests or raises more, they can be afforded better terms.)
A Favored Nations deal protects you in case you forget to ask for a certain perk. If another Co-Producer asks for that perk, then you'll get it as well. But be sure to check to see if the Favored Nations provision offered to you covers all perks or just the financial terms.

Since Co-Producer deals can vary and are subject to more negotiation than a standard investment, you should consider hiring an attorney or consultant to advise you on your agreement.

WHY CO-PRODUCE?

There are several reasons why investors graduate to becoming Co-Producers, most of which are similar to the reasons for investing, just on a higher scale.

AWARDS

One of the most significant advantages of Co-Producing compared to investing is Tony Award eligibility. Any name above the title is eligible for a Tony Award, the highest achievement one can earn in the Broadway theater. Tony Award eligibility is probably the second most important reason why Co-Producers choose to risk additional capital or raise money for shows (the first being that they love the show itself).

There have only been seventy Tony Awards for Best Play awarded in history. If you are a Co-Producer on the next Tony Award winning Best Play, you are immediately in a very exclusive club. That kind of status is priceless and can be used in a number of ways, including advancing your own theatrical career.

And the Tony Awards are only one of the awards that celebrate the theater. The Drama Desk Awards, the Outer Critics Circle Awards, The Drama League Awards are just a few examples of many of the prestigious awards that Co-Producers are eligible for. Adding "nominee" or "winner" to your resume can be a terrific status building credit.

FINANCIAL

Co-producing can be a fun and lucrative "side hustle." I know many Co-Producers who started co-producing as a hobby because of their love of the theater. Some people sell stuff on Etsy, flip houses, and some people Co-Produce! They organize funds from their networks and/or invest some of their own and became Co-Producers with the hope that the shows they produce recoup. They then earn the financial perks we discussed above, while also supporting the art that they love.

NETWORKING

While investing does get you some networking opportunities, Co-Producing is networking on steroids as you will get so much more intimate access to the artists, the other Producers, as well as some of the most influential people in our business. The individuals you'll meet as a Co-Producer will look at you much differently when you say you're a Producer as opposed to just an Investor.

Having the word "Producer" on your resume also gives you a status in the business and social world that few have attained. It separates you from others when applying for jobs, schools, country clubs, etc. Just expect people to start giving you scripts!

IT'S A PATH TO BECOMING A LEAD PRODUCER.

When I started producing on Broadway, I started as a Co-Producer. I knew that eventually I wanted to be a Lead Producer, but I wanted to be around the table first as a Co-Producer so I could learn from other Lead Producers. Even though I had a tremendous amount of experience on the staffs of Broadway shows as a Company Manager and General Manager and had even been a Lead Producer Off Broadway, I wanted a chance to sit with great Lead Producers to learn from their leadership and to be "in the room where it happens," before I was the one making all the decisions. (As a Co-Producer I would often play a game with myself I called, "What would I do," when the Lead Producer was faced with an important decision.)

If you look at the credits of most of the Lead Producers on Broadway today on the Internet Broadway Data Base (IBDB.com), you'll see most started as Co-Producers before they were Lead Producers.

The education offered by Co-Producing is priceless; I often say it's like theater-producing graduate school. And Co-Producing is one of the best way individuals can participate in the highest level of producing on Broadway, without giving up their day job. It's how I got started, even though I had a tremendous amount of experience from my decade of experience managing shows.

(Because Co-Producing has become so popular, I created a webinar that goes into many more details about Co-Producing, including examples of the financial arrangements, the legal documents required, and how to go about raising money, etc. The free webinar is located in our online appendix at www.TheProducersPerspective.com/appendix.)

A NOTE ABOUT RAISING MONEY

Many Co-Producers look to raise money for their shows because this allows them to get involved in more productions and diversify their own personal investments as well as their investors'. Raising Money for the arts is a challenging endeavor that I could write a whole book about it. Oh wait. I did write a book about it! It's called *Raise It*, and it details the systems and strategies I've used to raise over $50 million dollars for my productions. A link to *Raise It* is in our online appendix at www.TheProducersPerspective.com/appendix, as are other resources for those of you looking to start Co-Producing.

QUIZ!

1. If your name is above the title of a Broadway show as a Co-Producer, you will be eligible for . . .
    a. A Tony Award
    b. A Drama Desk Award
    c. An Outer-Critics Circle Award
    d. Additional profit depending on your Co-Producer deal
    e. All of the above

2. True or False: Co-Producers must invest all of their own money.
    a. True
    b. False

3. What is one of the most important clauses in your Co-Producer agreement?
    a. Financial
    b. Billing
    c. Opening Night
    d. Access to Rehearsals
    e. Favored Nations

ANSWERS: 1(e), 2(b), 3(e)

Advanced Strategy #2

"Front Money" Or Development Capital

I always know when I am talking to a seasoned Investor when after hearing about the risks of investing on Broadway they ask, "Is there a way to invest and get a *larger* return?"

While Co-Producing offers these Investors a chance to earn additional profit for more capital, some investors want an even greater return, which is when I introduce the concept of **Front Money.**

Front Money is the equivalent of "seed money," and is capital that is invested very early in the development of a new project, sometimes when there is nothing more than an idea.

Because the money is invested at such an early stage, it is an exceptionally high risk. And when I say exceptionally high risk, I mean it doesn't get any riskier! Why? Because usually Front Money is raised by Producers before there is a script! There may not be a director, a star, a theater or anything.

So, what is an Investor investing in when they invest Front Money? Two things:

1. The potential of the concept
2. The Lead Producer

Since there isn't a guarantee that the show will ever even get to opening night, the Investor has to feel confident in the idea but also that the Producer will get it from concept all the way to opening night, which might be years away! Because if the show does NOT get to opening night, it will most likely result in a complete loss of the Investor's money.

WHAT DO YOU GET FOR THIS TYPE OF RISK?

So, with all that risk, why would someone invest? Because Front Money Investors traditionally receive the best return on an investment you can get in the theater: a "1 for 1" deal.

Because this is the riskiest capital Producers accept, it makes sense that Producers give these Investors the best deal. Using the example in the previous chapter on Co-Producer Deals, instead of our Co-Producer Jane receiving $5,000 as a "kicker," if Jane was a Front Money Investor who was afforded a "1 for 1" deal, she would get $10,000.

If you remember, that $10,000 is the same amount that her investors received, which is why this is called a "1 for 1" deal. The return from the Investors' sides and the Producer's side is the same. Therefore, her total return in this example would be $20,000.

Under a "1 for 1" deal, the Producer is giving up 100% of his/her profits from this investment. (This is why Producers usually limit Front Money investments to 10% or less of their production, because too many Front Money Investors can eat up a Lead Producer's potential profits.)

When Front Money investing works, it can be very rewarding for an Investor. For example, on one of my shows, I called four people and said, "I have an idea, want to invest?" (Ok, it was a little more involved than that!) They did, because they believed in my idea, AND they believed that I would execute the idea. Whereas the regular investors earned approximately 450% on their money on that production, the Front Money Investors doubled that return and received almost 900%! Not bad, huh?

Again, Front Money Investing is exceptionally high-risk, and because of the gestation period of new musicals especially, the money can be tied up for a long time.

That said, several of my Investors actually *prefer* investing front money. I asked one of my regular Front Money Investors why they were drawn to this type of investing, despite the risk, and they said, “Ken, if I’m going to invest money in a high-risk venture, when I know there is the chance I could lose it all, why not invest when I can at least get double the return! It actually decreases my risk, not increases it, because the amount I can lose is the same.”

If you believe in your Producer and the idea and are looking for a way to maximize your returns while investing in Broadway, Front Money investing may be for you.

TIP: Front Money Investors are held in high regard by Lead Producers since developmental capital is vital to a Producer’s success, since not many Producers can afford to bootstrap their productions. So, as a Front Money Investor you should get early access to readings, as well as creative input and more. Make sure you ask for additional perks for your early investment. And additionally, I always give my Front Money Investors an option to become a Co-Producer on a show they invest in before I make that offer to others. This can be a major advantage. Imagine this . . . you invest in the creation of a new play by an unknown author (super high risk) and then three years in, Hugh Jackson decides he wants to start in that play. If you have the right to increase your investment, you can increase your returns. Use your early investment to your advantage when negotiating your future participation.

WHAT IS FRONT MONEY USED FOR?

Sometimes, since Front Money is raised so early in a show's developmental process, you may not be given a budget when offered a Front Money investment opportunity. However, you always can and should ask for a breakdown of how the money will be spent.

Usually, the funds are used for the following expenses:

- Lawyer (negotiation of rights, authors agreement, etc.)
- General Manager (creation of budgets, etc.)
- Advances for Author, Underlying Rights Holders, etc.
- Casting Director (especially if you are looking for a star)
- Readings and Workshops

Front money is the "R&D" (Research and Development) phase for a new play or musical so make sure the money is being spent on those kinds of activities.

THE FRONT MONEY AGREEMENT

The Front Money Agreement is a simple two or so page document that is designed to provide the necessary information for your investment with an emphasis on ease-of-execution. (We've included a sample in our online appendix at www.TheProducersPerspective.com/Appendix.) It was created to give Producers a way to start companies (shows) without the large legal expense or regulation that a full offering requires.

While most Front Money Agreements are similar to the agreement in our appendix, please do read anything you are offered thoroughly before signing and ask an expert (lawyer, consultant, etc.) to examine it before you sign on the dotted line. Remember, it is the highest risk capital in the theater and deserves even more scrutiny than a traditional investment, which has much more oversight.

OTHER FORMS OF DEVELOPMENT CAPITAL

The road to Broadway can be a long one. It is not uncommon for all shows, and especially musicals, to take several years to make it to The Great White Way. *Hamilton* took eight years to develop (and I think it was worth the wait, don't you?)

Most shows, especially musicals, have development productions or "tryouts" along the way to Broadway. Only two of the Tony Award-winning Best Musicals of the last twenty years did NOT have tryout productions before their Broadway premiere.

(If you'd like to learn more about the road to Broadway, especially if you have a show *you'd* like to get to Broadway, check out the free webinar entitled *The Path To Production.* A link is included in our appendix at www.TheProducersPerspective.com/appendix. In this webinar, I detail the many different steps a show takes as it develops, from reading to workshop to "out-of-town tryout" and eventually to Broadway.)

These different stages often offer different types of investment opportunities for Investors. In general, I consider there to be three tranches of fundraising on my shows.

1. Front Money
2. Developmental Money
3. Final Money

We discussed "Front Money" in the previous section, which is generally raised on an idea or concept, or before any major elements of the production are in place. "Final Money," which is the most common type of Broadway investment and pays out at the standard rates discussed in the earlier chapters of this book, is raised when a show is slated for Broadway. This is the most common and standard form of Broadway investing and the types of opportunities you will encounter the most.

Between Front and Final is what I call "Development Money," which I define as capital that is raised when there are major elements in place (script, score, Director, etc.) and an out-of-town tryout, non-profit tryout or workshop production planned. This type of investment traditionally pays out at a higher rate of return than Final Money (generally speaking around "1 for 2," regardless of the amount invested).

The reason for the higher payout is that the investment is still very high-risk capital, since a full production of the show usually has not yet been produced and therefore we don't know how the audience will respond. Additionally, there is still no guarantee that the show will get to opening night on Broadway. If the show isn't well received out-of-town or in workshop or wherever the show is being developed, then the Producers may decide to cut their losses and abandon the production. If so, your investment might be lost without you being able to attend the opening night on Broadway.

That said, investing Developmental Money is not as risky as Front Money since you can read a script, hear music, see who is attached to direct, etc.

Developmental Money is a good option for those seeking a higher return and for those interested in watching a show develop, without the higher risk of Front Money.

TIP: When negotiating a Developmental Money deal, make sure you ask for the right to be a Co-Producer when the show comes to Broadway, just like I recommended to Front Money Investors. Developmental Money is still challenging for Lead Producers to raise, so if you make this investment, you should get this additional benefit. You want to be ready to take advantage if the show debuts out of town and is the next *Jersey Boys*!

In the traditional business world, a Priority Loan is often referred to as a Bridge Loan. It's capital that is provided *after* the official offering for the production has closed, and therefore no more money can be officially raised under that offering.

If a show finds itself running out of money to cover its weekly expenses, and the Producer believes that the show may turn around, he or she may seek a Priority Loan to provide an infusion of cash to cover weekly losses, pay for additional advertising, etc.

Priority Loans are commonly used when a new show hasn't taken off yet, but word of mouth seems positive and the Producer thinks sales will increase if the show can run for a longer period of time. Sometimes a Producer will use a Priority Loan to cover losses in order for a show to be able to run until a major event like the Tony Awards, or to a holiday period, if the Producer thinks those events may help turn the production around or earn back some of the losses or loan.

The most famous example of a successful Priority Loan was on the original production of *Thoroughly Modern Millie*. The show opened to mixed reviews and a particularly negative one from The New York Times. However, the race for the Tony Award for Best Musical that year was basically between two shows, *Thoroughly Modern Millie* and *Urinetown*. Rather than close, the very smart Producers raised additional funds for advertising and to cover any potential losses before The Tony Awards, because they saw a potential turnaround in the near future and they believed they had a good chance of winning the Tony Award. Their bet paid off. *Millie* won the Tony which instantly altered the trajectory for the show. It later recouped and is now performed around the world.

Priority Loan money usually does NOT come with an additional return. It is generally provided by Investors, Producers or Partners of the show who are not yet ready to see the show close, so they put up additional funds to protect their original investment.

Priority Loan money is paid back FIRST however, putting the Priority Loan Investor in the best position for a return of their capital. So, should the show turn around, the traditional Investors (including Front Money Investors and Developmental Capital Investors) will have to wait for any return of capital until the Front Money investors are paid back in full.

The reason Priority Loan money is paid back first is because while the show has not closed or been abandoned, the money is considerably high risk, since the show is usually losing money, reviews have been published, and very few shows have turned themselves around from this position. Priority Loan money is even riskier than Front Money.

While you can try to negotiate better terms for providing a Priority Loan, I have never seen any financial benefits for anyone providing this type of loan other than first position payback. However, you could and should try to use your Loan to negotiate access to future shows, or a larger percentage of future shows, etc.

You should only loan a show funds if you are extremely passionate about the show and view the loan as a protective hedge on your original investment. And remember, if you are asked to make a loan to a show you are already invested in, <u>you can always say no</u>. Don't succumb to the peer pressure of investing more money if you think the loan is spending "good money after bad." If you don't believe there is a chance to at least recover the Front Money, then save that money for another production.

On the Jason Robert Brown musical *13*, my first Broadway show as a Co-Producer, we were asked to collectively contribute money towards a Priority Loan fund in order to get us to the holiday season which would help brand the show for licensing. We did, because the projections from the General Manager demonstrated that we would get the loan back. We did get the loan back and the show benefited from several additional weeks of performances.

It's important for traditional Investors to understand the concept of Priority Loans, because any show that takes a Priority Loan delay payback to its Investors. If the show does NOT turn around after the loan and closes, any additional revenues (stock and amateur, movie rights, etc.) will be paid back first to the individuals who made the Loan. This is why Lead Producers have to be very smart about when they take on such a Loan.

In my opinion, if a Producer takes a loan to keep a show open for emotional reasons, this is a disservice to the Investors, since it puts any chance of a capital return at great risk.

TIP: Ask your Lead Producer about their history with loans. How often have they taken them? Under what circumstances? What show? Did it work? This will tell you a lot about their producing style.

QUIZ!

1. What are the best financial terms you can get on a production?
    a. 1 for ½
    b. 1 for 1
    c. 2 for 3
    d. 6 for 6
    e. 8

2. In general, what stage of investment is the riskiest?
    a. Before a script
    b. After a reading, before an out-of-town tryout
    c. After the cast has been announced
    d. During previews
    e. They all have the same levels of risk

3. What are the most typical terms for a Priority Loan
    a. 1 for 1
    b. A 10% profit kicker on the tour
    c. Additional investment equal to the loan on the London Company
    d. First position payback
    e. Same as any Investor

4. What could Front Money be used for?
    a. An advance payment to an Author
    b. Legal fees
    c. General Manager fees
    d. Research on the subject matter on which the show is based
    e. All of the above

5. In general, what stage of investment is the riskiest?

a. Before a script
b. After a reading, before an out-of-town tryout
c. After the cast has been announced
d. During previews
e. They all have the same levels of risk

6. What are the most typical terms for a Priority Loan?
    a. 1 for 1
    b. A 10% profit kicker on the tour
    c. Additional investment equal to the loan on the London Company
    d. First position payback
    e. Same as any Investor

ANSWERS: 1(b), 2(a), 3(d) 4(e), 5(a), 6(d)

Conclusion

Congratulations. You have now completed more of an education on Broadway investing than most Investors who are already investing! You are armed with the basic information you need to begin investing with the hope of beating the market and finding the next big hit.

And I hope I've dispelled any myths or misconceptions you had about investing in the theater, and that you realize that Broadway, while risky, is a business like any other. And the best way to succeed in it or in any business is through proper education, due diligence, and, of course, passion for the business itself (which I know you have!).

And as you enter the world of Broadway investing, please remember the most important takeaways from this book:

1. Broadway Investing is a high-risk venture and there is always the possibility of losing your entire investment.

2. That risk can be mitigated through a systematic process of screening shows, diversification, as well as through other non-financial returns.

Now the last thing is . . . well, look, let me state the obvious. Do I want you to invest in the theater? Of course, I do! For those individuals with a passion for the theater and the patience and perseverance you need as you search for the big hit, investing in Broadway shows can be an emotionally, artistically, and yes, a very financially rewarding proposition.

There is nothing more rewarding than finding a way to turn something that gives you as much pleasure as the theater into something that also makes money.

That's why I call investing in Broadway, "The riskiest investment you'll ever love to make."

But here's why I'm different. I *only* want you to invest in Broadway if investing is right for you.

Because it is certainly not for everyone.

Hopefully this book has helped you decide if investing is for you. And if it's not, that's ok too . . . just promise me you'll invest in a lot of theater tickets instead.

But if it IS for you, then I encourage you to take another step and reach out to a Producer to get more information about investing in a show. It doesn't hurt to ask. Remember, there is never any obligation. And you will learn more just from inquiring.

If you have questions along the way, I'm here for you. Or even if you need a connection to someone you want to invest with. You now "know someone." Just drop me a note at ken@theproducersperspective.com and I'll be happy to help however I can.

And then, when the right opportunity comes along, and you are comfortable with the risk, give it a go. The next *Hamilton, The Lifespan of a Fact, Jersey Boys, Stomp, The Phantom of the Opera, The Lion King, Blue Man Group, Boys In The Band, The Band's Visit, Springsteen on Broadway, Latin History for Morons, Hello, Dolly!, The Play That Goes Wrong, Come From Away, Sunday in the Park with George, Dear Evan Hansen, The Front Page, Oh, Hello, An Act of God, Waitress, The Humans, School of Rock, Fun Home, An American in Paris, The Audience, Fish in the Dark, The Elephant Man, The Illusionists, The*

River, It's Only A Play, The Curious Incident of the Dog in the Night-Time, Hedwig and the Angry Inch, Of Mice and Men, Lady Day at Emerson's Bar and Grill, A Raisin in the Sun, Les Misérables, All The Way, Beautiful, A Gentleman's Guide to Love and Murder, The Glass Menagerie, Pippin, Matilda, Kinky Boots, Lucky Guy, Vanya and Sonia and Masha and Spike, Cinderella, Glengarry Glen Ross, The Heiress, One Man, Two Guvnors, The Best Man, Once, Death of a Salesman, The Mountaintop, The Book of Mormon, Fences, Red, A View From the Bridge, Race, A Little Night Music, Memphis, Next to Normal, Rock of Ages, Hair, Billy Elliott, In The Heights, August: Osage County, A Bronx Tale, Grease, Spring Awakening, A Chorus Line, The Drowsy Chaperone, The Color Purple, Sweeney Todd, Glengarry Glen Ross, The Light in the Piazza, Doubt, Twelve Angry Men, Wicked, The Boy from Oz, Avenue Q, Hairspray, Private Lives, Mamma Mia, Urinetown, 42nd Street, The Producers, The Full Monty, Proof, etc. is out there.

It’s up to you to find it.

And then invest in it.

Online Appendix

The following documents, whitepapers and webinars are all located on our free online appendix which can be found at www.TheProducersPerspective.com/Appendix.

- Front page New York Times article, "On Broadway, Investors with Shallow Pockets," about my crowdfunded production of *Godspell*.
- The 10 Myths of Broadway Investing
- Survey of Broadway Investors
- Whitepaper on Tax Changes for Broadway Investors
- New York Times Article on "Family Investing"
- Barron's Article on "Family Investing"
- Sample Broadway Offering Documents
- "The Long Chart of Grosses of The Longest Running Musical" Blog *about The Phantom of the Opera* and how the movie release affected its future.
- The Common Characteristics of Financially Successful Musicals infographic]
- Sample Broadway Budget
- Whitepaper on The Jobs Act
- "Do Tony Voters Forget The Fall" Blog re: The Odds of Getting A Tony Nomination in the Fall Vs. The Spring.
- NY Times Article on *A Gentlemen's Guide to Love & Murder*
- *Raise It*, Ken's Book on Raising Money
- Webinar on Co-Producing
- Sample Front Money Agreement
- Path to Production Webinar
- And more!